ESSAYS IN ISLAMIC MORAL ECONOMY: DEVELOPMENTALIST PROMISES, THE DELUSION OF FINANCIALISATION AND METHODOLOGICAL DILEMMA

by

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A Doctoral Thesis
Submitted in Fulfilment of the Requirements for the Award of
The Degree of Doctor of Philosophy at
Durham University

Durham University Business School

2018

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Abstract:

Islamic economics and finance emerged as a post-colonial counter-hegemonic attempt to develop a new economic paradigm based on Islamic normative principles and substantive morality, which could address the observed developmentalist failures of Muslim societies in a period where old colonial legacies had remained overwhelmingly shaping socioeconomic institutions in decolonized Muslim lands. It, hence aimed at redefining the meaning and function of human agency, land, labour and capital as well as the extended stakeholders in the Islamic social framework to generate a participatory and sharing economy. In doing so, Islamic economics is envisaged to eliminate the dependence upon capitalist formation of economic life and help to construct a new social formation of Muslim societies, beyond only economics and finance as single projects, in the light of Islamic ontology and epistemology.

In parallel with the normative aspects, Islamic finance and banking institutions were established as a peculiar mode of finance which is motivated by a religious concern of facilitating an alternative financial system that is constructed by Islamic principles, values and norms. According to such a construct, Islamic financial institutions (IFIs), therefore, are envisaged to circumvent social imbalance triggered by interest issue and generate particular modes of production by positing 'profit and loss sharing' and 'risk-sharing' operations of financing within the umbrella of 'sharing and participative' nature of Islamic moral economy paradigm through redefining capital through the Islamic financial prohibitions and screenings.

This research aims at developing a critical perspective in examining the performance of Islamic banks in terms of development promises and outcomes as essentialised by Islamic moral economy. It also aims to extent the analytical perspectives on the factors and paradigms preventing such consequences to be borne out of Islamic finance such as financialisation, as an operational consequence, and miss-defined *maqasid al-Shari'ah*, as an underlying methodological premise. In responding to the general aims of this research, three essays are developed.

The first essay aims to go beyond essentialising growth-based economic theories and explores the economic development impact of Islamic banking through discursive and empirical analyses. It aims, hence, to unearth to what extent aspirations of Islamic economics match up with its practical outcomes, which essentialises developmentalism as an objective and Islamic financial institutions as institutionalised forms of epistemological knowledge. Together with the discursive analysis in generating 'Islamic developmentalism', an empirical analysis is employed with a quantitative methodology through measuring and comparing performances of Islamic banks with an unbalanced panel of 21 cross section of countries observed during the period 2003-2014.

The second essay takes account of divergence from developmentalist ideals of Islamic economics empirically examined in the first essay, and hence delves into the dimensions of social failure of Islamic banks. As a response, among others, it relates the observed failure of Islamic banking in relation to the imagination of Islamic moral economy to 'financialisation' phenomenon. As the idea of Islamic economics was burgeoned at this stage of capitalist world system with the essentialisation of Islamic finance, this study argues, is a product of post-colonial discourse between religion and finance that was inspired by financialisation phenomenon. This chapter, therefore, aims to challenge the observed and developing financialisation of Islamic financing as an attempt that is invariably fictitious in nature leading to further disembeddedness and expansion of capitalist hegemony under the Islamic guise. Accordingly, it deploys a critical discourse analysis on financialisation within Islamic political economy frame by giving particular attention to the exploration of Islamic financialisation. In doing so, Polanyian understanding of embeddedness is adopted to address how Islamic financialisation impacts on social formation of Muslim societies by creating commodification and disembedment through Islamic finance operations. Upon elaborating on the theoretical construction of Islamic financialisation and its discursive analysis in a comprehensive manner, subsequently, an empirical analysis is conducted by witnessing the practical aspects of Islamic finance as a financialising activity within Islamic economics paradigm. Thus, the empirical part evidences how Islamic finance engenders a financialised view of (Islamic) economics through its operations. Specifically, it examines the impact of the ascendance of

Islamic finance on financialisation trajectory of entire economy, with a panel of 14 Muslim-dominated countries covering the period of 2002-2014, to ascertain whether operations of Islamic finance, by and large, strengthen real economy or contribute to further financialisation in economies where domestic market share of Islamic finance reaches medium or high systematic importance.

Third essay argues that the social failure of Islamic finance in relations to fulfilling developmentalist outcomes and its negations of moral expectations is highly a methodological problem, not just an issue bounded with practical realities of the field. This essay, therefore, aims to suggest *maqasid al-Shari'ah* as the fundamental knowledge creation methodology for the theorisation of Islamic moral economy through which Islamic developmentalism conceptualised and transformed into public policy making. However, it criticises market-oriented understanding of *maqasid* as a *fiqhi* construct, which is extensively applied in Islamic finance as a legitimisation tool leading up to a new moral code of conduct for economic activities. In responding to this, this essay develops an authentic approach towards *maqasid al-Shari'ah* based on substantive morality beyond the instrumentalised meaning of *maqasid* and morality.

Based on the theoretical discussion and empirical findings, this research suggests that the objective of Islamic banking and finance should not be ensuring of the dominance of capital but rather to ensure that capital is working within the objectives of society whereby capital is de-centred. Considering that most of the Muslim societies and developing countries are in dire need of development, therefore, it is important as to how Islamic finance and banking can work to produce development and essentialise the interest of extended stakeholder as suggested by *tawhidi* paradigm. Therefore, this research expands the scope of non-developmental expansion of Islamic finance and its capital fundamentalism through the introduction of the notion of Islamic financialisation. It, accordingly, suggests Islamic developmentalism, founded in the theoretical framework of Islamic moral economy, as an embedded form of establishing distributive justice that facilitates paradigmatic shift towards an authentic theory of development, which can be facilitated by Islamic finance working within the 'essential goals of the society'. In achieving this, *maqasid al-Shari'ah* is essentialised as the fundamental knowledge creation methodology for the theorisation of Islamic economics through which Islamic developmentalism conceptualised and transformed into public policy making.

DECLARATION

I hereby declare that none of the material contained in this thesis has previously been submitted for a degree in this institution or any other institution. I further declare that none of the material contained in this thesis is based on joint research. The content of this thesis consists of the author's original individual contribution with appropriate recognition of any references being indicated throughout.

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Alhamdulillah, all praise to Allah, the most gracious and the most merciful for the guidance and blessing in actualising my goal to achieve this success in my studies.

This thesis is an outcome of hard work, challenges, support and other myriads of factors all of which motivated me to achieve such a success in my life. As the success does not origin from my effort only, I wish to express my gratitude to all stakeholders of this achievement for their support and contribution.

I must sincerely thankful to my supervisor, Professor Mehmet Asutay, for his continued support, endless and patient guidance, motivation, and encouragement during the thesis period. However, more importantly, I would also like to extend my deep gratitude to him since I learned various important values beyond the thesis writing to actualise in my life. Amongst many others, I witnessed how normative aspects of Islamic moral economy is characterised and practised as an individual in his everyday life and, in particular, in his relationship with me that breaks traditional student-supervisor boundaries and constructs an ungrudging relationship based on *ihsan*. The completion of this thesis, therefore, accompanies with a feeling of bittersweet happiness. I will always be indebted to him and forever grateful.

I must also thankful to my second supervisor, Dr. Ahmed Elsayed for his encouragement and criticisms during the thesis. In addition, I wish to express also my appreciation to Dr. Mahmut Zortuk and Semih Karacan for their direct and indirect assistance.

Apart from the academic support, a warm and friendly environment in the Durham University Business School and the Durham Centre for Islamic Economics and Finance played a major role in achieving the completion of this thesis. Thus, I must name and thank Harun Sencal, Erhan Akkas, Hajar Raouf, Banjaran Indrastomo, Turgay Kart, Sabri Mohammad, Alija Avdukic, Tareq Moqbel, Arman Mergaliyev, Amirul Haqeem Abd-Ghani, Ebi Junaidi, Aysenur Aydin, Mucahit Ozdemir, Badrerddine Bera, Ercument Aksak, Dr. Mohamad-Husam Helmi, Haris Macic, Mehmet Artik and Izzettin As amongst many others.

In terms of financial support, remembering the serious financial hardship I experienced and therefore could only find micro-scholarships from various local institutions in Turkey, I must thank to Bereket Foundation, Borsa Istanbul, Camlica Foundation, Ensar Foundation, and Turing Institution. My special thanks, in this manner, are for Temel Haziroglu, Metin Alpaslan, Davut Sanver, Hasan Gultekin, Talat Ulussever, Yusuf Varli, Seref Dursun, Hulusi Yigit and

Kemal Ozpinar. I should also put on record my appreciation of the funding I have received from the Humayon Dar Hardship Fund at the Durham Centre for Islamic Economics and Finance. Durham Centre for Islamic Economics and Finance and also Durham University Business School Doctoral Programme has also provided financial support for attending conferences.

I would also like to thank to Ugur Altun, Omer Mirac Yaman, Mehmet Babacan, Zafer Ozdemir and Mehmet Emin Babacan who continuously supported and assisted in educating me on the personal, professional or scholarly level for at least 15 years.

Finally, I shall always remain deeply indebted to my family; my dearest mother, Fatma Yilmaz, and my dearest father, Sebahattin Yilmaz, my affectionate sister and brother for their love, care and prayers; my mother-in-law, Guzin Yaman, and my father-in-low, Abdulvahap Yaman for their continuously pushing and encouraging me throughout the years whenever I needed them and whose support was vital for the completion of this thesis; my beloved wife, Elif Yilmaz, for her hard work, endurance and dedication; without her love, patience, motivation and support, I would not have been able to finish this thesis; and last but not least, for my sons Yusuf Tarik Yilmaz and Zahid Yilmaz for the laughter, happiness and joy they bring.

I pray that Allah bless all of you with His greatest bounties and rewards.

Isa Yilmaz

December 2018

CHAPTER 1

INTRODUCTION

1.1. RESEARCH BACKGROUND

The narrative of economic history constructed beyond Eurocentric perspective evidences that the characteristics of pre-modern formation of social life were shaped by moral dynamics including shared values, norms and beliefs, which resulted in embedding the functioning of social, economic, political and cultural institutions. The established and functioning embeddedness had thwarted the emergence and prevalence of self-regulated institutions reckless to the moral concerns raised by individuals; instead, it had paved the way for the essentialisation of societal development with moral concerns remaining at the centre of economic relations. In doing so, human interchange, and economic life in particular, had submerged in social relations, and society had organically enveloped its institutions, including economic policies and financing practices. The embedded economy, in this manner, we are told, had existed since archaic times, particularly in premarket system societies.

With the emergence of economics as a positive science and modern life including modern economic practices that brought out the market economy system, later, economic institutions substantially gave way to modern forms in which morality has been dislocated from the core of economic activities which ultimately bred a value-free notion of economics resulting into dis-embeddedness. As the transformation from value-loaded to value-free character of economy is adopted, economic objectives have also been exposed to some contextual alterations in order to bring them into conformity with the new aspirations of 'positive economics'. In doing so, essentialisation of capital as a factor of production and capital-intensive growth policies, nurtured by the Eurocentric approach, superseded developmentalist policies, which meant a narrowing shift from normative to positive dealing of the concept of development. The issues of poverty, unemployment, wealth generation, equitable distribution of income and wealth, and improvements in many spheres of public life, thereupon, have been tackled around this scant form of development.

The transition from moral economy understanding to self-regulated market economy derived from positivist ideology led to a counterhegemonic discourse by Western academics in the 19th century Europe, which later opened up the literature on moral economy and its use as a strong critique to capitalist economic system. The social protectionist movements emerged as a counter hegemony in the post-war period in the 20th century to respond to the unregulated nature of market economies resulting in, for example, the emergence of welfare state. Muslim scholarship, amid these developments, responded to capitalist penetration resulting in disembeddedness in a different manner in their attempt to reconstruct their societies in that the debates on Islamic morality and its articulation on modern economic institutions remained peripheral. However, the emergence of Islamic economics movement also coincides the global search for alternatives in different part of the world including in the West.

As the Muslim societies were facing a great deal of challenges, including international political power decline, prevalence of nationalist movements, an ever-increasing stream of liberal and secular worldviews and the effect of globalisation on the role of nation states in the 20th century, they strived either for adopting capitalist mode of production through imposition to establish a particular social formation that is alien to their respective societies (resulting a hybrid everyday practice with formal economy dominated with market rules at the centre while informal economy carried the traces of tradition in the periphery and semi-periphery), or they searched for an authentic Muslim identity that rejects Western values and norms, but contrarily, enables Muslims to reconstruct their own worldview in the modern era.

Although it was expected that the overcoming challenges and the aspirations of establishing authentic Muslim identity would bring the issue of Islamic morality into the centre of academic debate and everyday practice of economy and finance, it rather worked the other way around and culminated in a hybrid and malaise understanding of economic system which ruled out the flourishing of Islamic moral economy in the Muslim thought. The impacts of hybridity which has later been shaped by 'mimicry' and even 'mirroring', consequently, shaped the theory and practice of Islamic economics and finance in the modern Muslim world. As a result, Islamic finance as part of the Islamic economic movement, contrary to its claim, could not authenticate itself to be a novel outcome of Islamic ontology, for it became a variant of mainstream financial reality situated in the Western epistemological frame. In this, this study attempts to reconstruct Islamic economics affected by the same trajectory as it has mostly remained 'Islamization' of the concepts and theories of neo-classical economics, such as the utility vs Islamic utility regardless of re-defining if Islam suggests utility or perhaps such an intent can better be explained through *falah* process and *falah* function.

1.2. PROBLEM STATEMENT: EVOLUTION OF THE IDEA OF ISLAMIC ECONOMICS

Despite the state of art in Islamic economic modelling shows no way other than being an unfinished project and its Islamic finance arm showing social failure, the origins of Islamic economics initially envisaged a completely different system proposition. In this sense, the idea of Islamic economics burgeoned as a post-colonial counter-hegemonic attempt to address the observed developmentalist failures of Muslim societies in a period where old colonial legacies had remained overwhelmingly shaping socioeconomic institutions in decolonized Muslim lands. Since the prevailing legacies are considered to impede emancipation and empowerment of Muslim identity, which is the main objective function of Islamic methodology, obliterating their traces was seen an essential concern in developing an authentic meaning of economy and society as part of their identity search. Thus, Islamic economics emerged as a project to develop a new economic paradigm based on Islamic normative principles and substantive morality, which could respond to the challenges Muslim individuals and societies face with the mainstream materialistic and performing understanding of economy. Therefore, it aimed at redefining the meaning and function of human agency, land, labour and capital as well as the extended stakeholders in the Islamic social framework to generate a participatory and sharing economy.

Considering the ideational mismatches between Islamic and secular worldviews, Islamic economics is envisaged to be functioning to eliminate the dependence upon 'capitalist formation of economic life'[1] and help to construct a new social formation[2], beyond only economics and finance as single projects, of Muslim societies in the light of Islamic ontology and epistemology. In achieving this, in the short-run, utmost importance was given to public policy oriented developmentalist agenda with the objective of eliminating underdevelopment, eradicating impoverishment and weak politico-economic structures, while in the long-run an attempt was considered in developing Islamic social formation in which economic practice is considered to be submerged in a nexus of social relations.

[1] Capitalist formation of economic life refers to the organization of social and economic life through capitalist motivations in the sense of essentialising capital accumulation and centring capital and maximisation of shareholder value.

[2] Social formation is defined as "totality of instances articulated on the basis of a determinate mode of production" (Althusser and Balibar 1970:207), which is a Marxist concept used to describe the conditions for the existence of particular mode of production in constituting the social formation of the society. It simply implies the organisation of society which includes organisation of economics resources in generating a particular mode of production (Asutay, 2018).

The theoretically defined aspirations of Islamic economics are invariably welcomed and encouraged to put into practice, yet the historical evidence showed that the institutionalisation process has been limited to banking and financial activities with an unsophisticated and non-theoretical making of Islamic finance. The general trend of Islamic economic studies has thus been moving towards finance and bank centred view of Islamic economics in which financial operations constitute the pivot of economic activities. This is construed as divergence from ideals to the mimicry of conventional finance through representing hybrid financial services (Asutay 2007b, 2012).

The emerging need of an Islamic financial system had surfaced in the late 1940s when decolonization took place after the World War II. With this new stage of political history, previously colonized countries were allowed to design their own institutional structure without any political interference of colonial powers. From inner perspective, Muslim societies' confrontation with the existing social, cultural, political and economic articulations of Western worldview now transformed into a different phase where direct applications of Western strategies on Muslim lands were interrupted after the decolonization.

While boundaries of these lands are no longer invaded by Western colonialist powers and the ways of democratization and nation building has been expedited and 'liberalised', old colonial legacies have still been prevailing and shaping social and economic structure of these underdeveloped world. This has caused a particular form of dependence that was conceptualised with 'neo-colonialism' – a term coined by Nkrumah (1965) - under which the former economic and cultural relationships of direct colonization period are maintained through different means in disguise of economic cooperation, global culture, development *etc*. Islamic economic movement and its finance articulation, under such circumstances, emerged to play an important role in authenticating Muslim nation building in economics and public sphere through the advantages of decolonization; however, it had to come up against the prevalent economic structure in the following years of its establishment.

Along with the historical and political effects rooted in its emergence, technically speaking, Islamic finance and banking, the main institutions emerged from Islamic economics movement, embraces a peculiar mode of finance which grounds its theoretical underpinnings to Islamic economics paradigm, and hence, undertakes to operate within the ambit of Islamic legal rules and moral obligations. As can be inferred, it is motivated by a religious concern of facilitating an exclusive financial system that is constructed by Islamic principles, values and norms. Contrary to the interest-based nature of global financial system through which exorbitant profits are realised at the expense of impoverishing rest of the world, Islamic financial institutions (IFIs) aim to circumvent social imbalance triggered by interest issue and generate particular modes of production by positing 'profit and loss sharing' and 'risk-sharing' operations of financing within the umbrella of 'sharing and participative' nature of Islamic economy paradigm. The prohibition of *riba*, in this sense, refers to a new mode of production within Islamic social formation, in which the dominance and hegemony of capital is removed; instead, capital is treated equal with the rest of the stakeholders (Asutay 2018). In other words, the removal of interest from economy is nothing but the rule against the domination of capital in terms of unfair return of capital leading to preserve each stakeholder's right in the production process and financial area. This, hence, creates opportunity space for other stakeholders to flourish, emancipate and empower through providing equal opportunities (*see*: Asutay 2017); and hence the entire process aims at multidimensional development. Therefore, Islamic political economy features profit and loss sharing and risk sharing in the form of equity financing in shaping Islamic finance as the main thrust of expanding stakeholder for development by providing accessibility to resources (Asutay 2013).

Established over four decades ago and proliferated in a short span of time across the globe, Islamic finance, at its state of art, is extolled for its performance to show an unprecedented success in achieving a continuous growth in terms of asset size, and for its financial services reaching an overall total value of $1.893 trillion as of 2016 (Islamic Financial Services Board (IFSB) 2017:7). Despite the share of Islamic financial assets ($1.893 trillion) remains only 1% of the global financial market of $127 trillion (Ernst and Young (E&Y) 2016), IFIs are increasingly becoming part and parcel of the global financial system. This, in return, leads to the expectation that the momentum gained with Islamic finance should accompany with economic wellbeing across its operating fields due to the fact that financial development would necessarily foster economic growth and generate welfare in a wider sense.

While Islamic finance secures its position in the global financial order by introducing new products and permeating through un-tapped fields, its distinguishing feature of being a religion-based proposition – rather than self-regulated market system - engenders some challenges in integrating into global, secular, modern and capitalistic characteristics of mainstream finance. This is due to the reason that Islam attaches certain principles to financial activities such as prohibitions of *riba*, *gharar* (excessive uncertainty) and *maysir* (gambling), whereas conventional financial markets trust self-regulation without reliance on divine knowledge to lead its activities. This obliges Islamic finance scholars to adopt either an authentic but necessarily non-globalised financial practice within the boundaries of Islamic law, or hybrid practices and institutions that mimics conventional finance but performs relatively more efficient with its dubious activities in terms of being complaint with Islamic legal and moral rulings.

Remembering ethical principles embedded in its foundational premises of Islamic economic, Islamic finance emanating from such a source is also expected to generate developmentalist consequences in such a challenging atmosphere. Developmentalism as a social objective in financial activities of Muslim societies was mainly essentialised by the founding fathers of Islamic economics, who consider Islamic finance to be value (ethically) and norms (morally) driven industry that has to exhibit thriving 'social performance' as well as financial performance (*see*: Mannan 1970; Chapra 1979; Zarqa 1980; Siddiqi 1981; Choudhury 1986; Ahmad 1994; Naqvi 2003 amongst others). Examining its economic performance over the years, it can be somewhat asserted that IFIs are financially performing moderate (Hassan and Aliyu 2018); however, while developmentalist contributions are reckoned with, they lag far behind the aspired level as identified by Islamic moral economy and failed to accommodate enhancing social good for which they were initially considered. As Islamic moral economy aims at re-defining capital and its role in economic and financial activity, Islamic finance has taken the capitalist or neo-classical definition of concepts and forms of practice. Therefore, it is claimed that Islamic finance has given up the equity-based formulation of Islamic moral economy for 'efficiency of capital' based paradigm of neo-classical economics and financialised practices.

1.3. RESEARCH AIMS, QUESTIONS AND METHODOLOGY

As discussed in the preceding sections, this research aims to deconstruct and analytically explore some of the essential issues mentioned. The essays in this research, thus, aims at developing a critical perspective in examining the performance of Islamic banks in terms of development promises and outcomes as essentialised by Islamic economics. It also aims to extend the analytical perspectives on the factors and paradigms preventing such consequences to be borne out of Islamic finance such as financialisation, as an operational consequence, and miss-defined *maqasid al-Shari'ah*, as an underlying methodological premise.

Since this research is presented in three-essay-based format (two empirical and one discursive), the aims, objectives, research questions and methodology for each essay are presented as follows:

Essay 1: Islamic Banking and Development: Revisiting Developmentalist Promises of Islamic Economics

In an attempt to critically evaluate conventional notion of economic growth and development with the resultant imbalances it creates, the first essay aims to go beyond growth based economic theories and explores the economic development impact of Islamic banking through discursive and empirical analyses. It aims, hence, to unearth to what extent aspirations of Islamic economics match up with its practical outcomes, which essentialises developmentalism as an objective and Islamic financial institutions as institutionalised forms of epistemological knowledge.

In line with the stated aims, initially, a conceptual framework for Islamic developmentalism is constructed to identify the distinctions and dimensions of development, thereby, 'developmentalism' is brought out as the essential operational model of Islamic banking as envisaged in the emergence of Islamic economics and finance discourse. This is followed by an empirical analysis by employing a quantitative methodology through measuring and comparing performances of Islamic banks with an unbalanced panel of 21 cross section of countries observed during the period 2003-2014; thereby, it seeks potential contributions of Islamic banks on economic development trajectories of Muslim-dominated countries based on the predefined notion of 'Islamic developmentalism[3]'. The underlying assumption, here, is that Islamic financial performance should not be confined to financial area only, as due to their moral construct they should be subjected to 'social evaluation' in the sense that Islamic moral economy locates Islamic banks as institutions of contributing to the social good or *ihsan*.

In relation to the aims and objectives, following research questions are developed:

RQ_1: Why does going through finance-growth nexus remain incapable in exploring the impact of finance on socioeconomic goals of countries?

RQ_2: What is the particular imagination of Islamic moral economy in relation to development paradigm?

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[3] This study recognizes the value-loaded definition of 'developmentalism'. However, it also recognizes that Islamic aim is not only economic development but multi-faceted development within the parameters of *adalah, ihsan, rububiyah and tazkiyah* in the context of *tawhidi* paradigm (Asutay 2013). Hence, developmentalism is redefined within Islamic normativeness by essentialising human-centred development by re-defining individual as Islamic economics "aims at the study of human *falah* achieved by organising the resources of earth on the basis of cooperation and participation" (Khan 1984:54). In this context, re-defined developmentalism is objected towards emancipation and empowerment in every aspect of life within the *ihsani* social formation.

RQ$_3$: In what ways does 'banking-development nexus' differ from 'banking-growth nexus'?

RQ$_4$: What are the most appropriate indicators accounting for Islamic banking growth and economic development?

RQ$_5$: To what extent does Islamic banking sector contributes to the developmentalist objectives in Muslim countries?

Based on the results produced in this essay, the following two essays aim to empirically and discursively address the sources of 'development impact' related failure of Islamic banking by locating it in the financialisation as an operational choice and misapplication of *maqasid* as a methodological base.

Essay 2: *Financialisation and Disembeddedness in Islamic Banking: Critical Discourse and Empirical Analyses on Performing Banking and Finance vs. Islamic Moral Economy*

The second essay takes account of divergence from developmentalist ideals of Islamic economics empirically examined in the previous essay, and hence delves into the dimensions of social failure of Islamic banks. As a response, it relates the observed failure of Islamic banking in relation to the imagination of Islamic moral economy to 'financialisation' phenomenon – a flourishing concept in the heterodox literature - which represents a systemic transformation of capitalist economies during the last few decades that brought about a sharp divergence between economic and financial activities in favour of dominance of finance in the face of performing productive economy as part of the shift towards finance-led capitalism. As the idea of Islamic economics was burgeoned at this stage of capitalist world system, its essentialisation of Islamic finance, this study argues, is a product of post-colonial discourse between religion and finance that was inspired by financialisation phenomenon. Thus, one cannot expect developmentalist objectives from Islamic financial institutions in an environment of financialised economy, for financialisation is itself a project of eliminating human in economic relations through submerging human interaction in a nexus of financial relations.

It is argued, hence, that the emergence and systematic institutionalisation of modern Islamic finance industry in 1960s was not a coincidental development, but rather highly influenced from the essentialisation of finance dominated economic system. Thus, Islamic finance could only become an in-paradigm alternative within debt-based economic environment. This chapter, therefore, aims to challenge the observed and developing Islamic financialisation as an attempt that is invariably fictitious in nature and is a government-led top-down process in most of the countries where Islamic finance is visible, rather than an outcome of bottom-up demand for Islamic social services.

Along with this, it suggests an Islamic political economy approach to financialisation through which the nature, evolvement and burdens of financialised economies together with its implications on individual and social life are reconsidered in the light of Islamic ontology and epistemology. Accordingly, it deploys a critical discourse analysis on financialisation within Islamic political economy frame by giving particular attention to the exploration of Islamic financialisation. In doing so, Polanyian understanding of embeddedness is adopted to address how Islamic financialisation impacts on social formation of Muslim societies by creating commodification and disembedment through Islamic finance operations.

Upon elaborating on the theoretical construction of Islamic financialisation and its discursive analysis in a comprehensive manner, subsequently, an empirical analysis is conducted by witnessing the practical aspects of Islamic finance as a financialising activity within Islamic economics paradigm. Thus, the empirical part would evidence as to how Islamic finance engenders a financialised view of (Islamic) economics through its operations. Specifically, it examines the impact of the ascendance of Islamic finance on financialisation trajectory of entire economy, with a panel of 14 Muslim-dominated countries covering the period of 2002-2014, to ascertain whether operations of Islamic finance, by and large, strengthen real economy or contribute to further financialisation in economies where domestic market share of Islamic finance reaches medium or high systematic importance. Accordingly, it employs a quantitative methodology and makes use of secondary data with an unbalanced panel data analysis. A range of econometric techniques are utilised including pooled OLS, random effect and system-GMM estimators to address heterogeneity, over-identification and endogeneity issues.

In relation to the aims and objectives, the following research questions are developed:

RQ_1: What are the historical dynamics behind the emergence of Islamic finance as a hybrid financial product and institution instead of an authentic alternative to global financial system?

RQ_2: In what sense does Islamic finance fail to operate beyond market economy understanding and becomes invariably disembedded and financialising economic practice?

RQ_3: What are the theoretical boundaries and scope of Islamic financialisation?

RQ_4: What are the institutional and practical implications of Islamic financialisation?

RQ_5: To what extent Islamic banking has contributed to financialisation in the countries it has certain presence?

Essay 3: Re-embedding Maqasid al-Shari'ah in the Essential Methodology of Islamic Economics

Based on the first two essays, third essay argues that the social failure of Islamic finance in relations to realising developmentalist outcomes and its negations of moral expectations is highly a methodological problem, not just an issue bounded with practical realities of the field. This essay, therefore, aims to suggest *maqasid al-Shari'ah* as the fundamental knowledge creation methodology for the theorisation of Islamic economics through which Islamic developmentalism conceptualised and transformed into public policy making. However, it criticises market-oriented understanding of *maqasid*, which is extensively applied in Islamic finance as a legitimisation tool leading up to a new moral code of conduct for economic activities. In responding to this, this essay aims to develop an authentic approach towards *maqasid al-Shari'ah* based on substantive morality beyond the instrumentalised meaning of *maqasid* and morality.

Beyond instrumental and eclectic approaches, this essay argues that the theoretical grounds of Islamic economics should be re-examined in the light of proactive *maqasid al-Shari'ah* framework with its nine dimensions, beyond the traditional Ghazalian *maqasid*, elaborated in the related section. By doing so, the rationale behind the failure of realising Islamic developmentalism in post-colonial Muslim nations can better be explained, since proactive *maqasid* envisages a totally different methodology and approach towards developmentalist considerations when compared to existing applications of *maqasid* based on methodological individualism. Morality, here, plays a central role on the entire process of knowledge authentication through *maqasid al-Shari'ah*, while the current use of *maqasid* in Islamic banking and finance demonstrates that it has been relegated to *fiqhi* injunctions and used as an instrument to legalise particular product and operation in a legalistically rational manner. Thus, substantive morality should be embedded through *maqasid* in the theoretical underpinnings of Islamic economics to generate substantive nature of Islamic moral economy in line with *maqasid* expectations as a distinct system of economy. This requires interpersonal and social relations not to be merely relegated to economic relations or relations between 'things', but economics and finance should be embedded into norms and values of society through locating ethico-economic relationship across each system so that morality can be articulated beyond impersonal market environment to generate Islamic moral economy.

Based on the aims and objectives, this essay raises the following research questions:

RQ_1: How should *maqasid* be designed in order to deliver an authentic and functional methodology for Islamic economics?

RQ_2: In what sense the prevailing *maqasid* perspective in Islamic finance facilitates its divergence from the aspirations of Islamic economics?

RQ_3: What are the consequences of the prevailing Ghazalian *maqasid* framework in relation to Islamic moral economy expectations?

RQ_4: What is the nature and constituents of an effective *maqasid* to embed Islamic morality in definition and operations of Islamic economics and finance?

1.4. RESEARCH MOTIVATION AND SIGNIFICANCE

Islamic finance is a significantly growing industry within the global financial system. Considering the motivation behind its emergence, it was institutionalised to fulfil the objectives of Islamic economics paradigm, and, hence, embraces a value-loaded character beyond the logic of conventional finance, which is driven by the market system with a value-free notion of efficiency and with the dominance of capital. Islamic finance is, hence, envisaged to generate both financial and social performance to contribute to the development trajectories of Muslim societies so that financing becomes an embedded activity in the process of producing social good. By doing so, Islamic financial sphere becomes submerged in a nexus of social relations and the accompanying ultimate goal of developmentalism.

The motivation of this research stems from the fact that Islamic banks, having the majority share in the Islamic financial sector, diverged from the initial aspirations and paradigm of development-oriented mode of financing elaborated above, and have converged towards mainstream financial system in the operational level, leading up to disembeddedness between finance, economy and society in a Polanyian sense. A thorough elaboration and systemic analysis about the hybridity of Islamic financial products and the mimicry of conventional financial framework, as the state of art in Islamic banking sector manifests, is required to shed light on the political economy dynamics of Islamic banking as a disembedded industry from the objectives of Islamic economics. In doing so, this research goes beyond the classical approach towards financial development, which takes accounts of growth-based dimensions of banking activities such as financial depth, access, efficiency and stability as observed in the World Bank perspective. Instead, this research takes the debate to one stage further by evaluating Islamic financial performance through its developmentalist contributions that necessarily consider social implications and articulations of financing. This study, therefore, suggests that the objective of Islamic banking and finance should not be ensuring of the dominance of capital but rather to ensure that capital is working within the objectives of society. Considering that most of the Muslim societies and developing countries are in dire need of development, therefore, it is important as to how Islamic finance and banking can work to produce development and essentialise the interest of extended stakeholder as suggested by *tawhidi* paradigm.

The recognition of the social failure, inductively, leads us to relate it to the notion of financialisation. In this manner, financialisation is considered to be the latest form of capitalist stage, and the emergence of Islamic finance together with its rise of 'financing' within Islamic economics paradigm has been influenced from such a political economy atmosphere. As finance has been dislocated from economic sphere, it gained an autonomous sphere with its own objectives devoid of real economy and in need of developmentalist perspective. Islamic finance, similarly, mimics the prevailing structure and the institutional logic of conventional finance and gives rise to the financialisation of Islamic finance through favouring 'finance as the ultimate objective' instead of 'finance for social good', the difference of which is clarified extensively in the following words of (Shiller 2012:7): "finance is not about 'making money' per se. It is a 'functional' science in that it exists to support other goals – those of the society. The better aligned a society's financial institutions are with its goals and ideals, the stronger and more successful the society will be", which echoes Chapra's position (2009).

Based on such historical developments of Islamic finance, this research suggests a proactive *maqasid* understanding based on substantive morality embedded in the theoretical underpinnings of Islamic economics to function as a substantial methodology in deriving developmentalist oriented public policy making. Thus, the theoretical grounds of Islamic economics and its articulation of Islamic banks are re-examined in the light of the proactive *maqasid al-Shari'ah* framework with its extended dimensions. This research argues that the roots of social failure of Islamic banks is a direct consequence of a more substantial problem related to methodology. Therefore, the neglect of methodology in theory making, in the case of articulating Islamic economics into policy level, sparked off the emergence of Islamic financialisation and hence brought dissociation of finance from Islamic developmentalism. Thus, due to being concerned with the observed convergence towards further financialisation of Islamic banking, this study aims to identify the process of financialisation and brings attention to the nature of financialisation taking place in Islamic banking.

The evaluation of the historical rise of Islamic finance industry from the Polanyian view of embeddedness makes this research significant, for it paves the way for considering practical aspects of Islamic economics beyond neoclassical discourse by bringing developmentalist consequences into question. It also conceptualises 'Islamic financialisation' as a broader phenomenon for development that needs to be addressed multifariously. With equal importance, this research makes contribution to the methodological issues around the theorisation of Islamic economics by introducing a new methodological approach based on Ibn Qayyimian understanding of public policy-oriented consequence. In doing so, this research argues that *maqasid al-Shari'ah* should be located as the essential methodology of Islamic economics. Thus, due to observing that the *maqasid* utilised in the practice of Islamic finance and banking would not produce development as a consequence, this research has taken up the task of re-defining *maqasid* and its constituents.

Considering that the developments in Islamic banking and finance have indicated its convergence towards conventional financial practices, this research should be considered as a novel attempt to identify the underlying reasons for such convergence through two particular sources: market forced financialisation and methodological incompleteness of the emergence.

1.5. OVERVIEW OF THE CHAPTERS

In Chapter 2 – *Islamic Banking and Development: Revisiting Developmentalist Promises of Islamic Economics*, the term 'development' is dissected thoroughly in a conceptual manner, and its impact on socioeconomic life is discussed where multifacetedness of developmentalism is pinpointed. The conventional understanding of growth and the wider concept of development is contrasted and compared with Islamic moral economy perspectives on developmentalism. After making a clear distinction between growth and development, developmentalism is accepted as the remedy for the unequal consequences and imbalanced growth orientation of many countries. Therefore, growth paradigm is critically analysed to suggest Islamic moral economy's developmentalist essentialisation. In doing so, some references are also given to the social failure of Islamic finance to reveal Islamic moral economy's vision for developmentalism.

After presenting a conceptual and theoretical discussion, an econometric analysis is conducted to explore the relationship between Islamic banking growth and economic development. In doing so, possible explanations for the impact of growth of Islamic banking industry on the quantitative aspects of developmentalist oriented aims is sought through the empirical analysis with an unbalanced panel of 21 cross section of countries for the period of 2003-2014. A development index highlighting the quantitative parameters is considered to test the performances of Islamic banks with regard to their promotion towards individual wellbeing and social welfare. For the outcome, the resulting trends show that Islamic banks do not have significant effect on economic development patterns of countries, implying a poor performance that necessarily resulting into social failure.

Chapter 3 – *Financialisation and Disembeddedness in Islamic Banking: Critical Discourse Analysis and Empirical Evidence on Performing Banking and Finance vs. Islamic Moral Economy* – is based on the consequences of discursive and empirical analyses in Chapter 2. The econometric analysis in the first essay is expected to expose the observed developmentalist failure with regards to Islamic banks' performances. In an attempt to reveal underlying causes of development or social failure, the phenomenon of financialisation is examined both in conceptual and empirical aspects to relate the failure with the ascendance of finance centred view of economy, which shows the most recent phase of capitalist mode of production. It is, therefore, argued that social failure of Islamic finance pertains highly to financialisation and hence to the domination of capital.

Together with the distinguishing aspects of financialisation discussed by various approaches, this chapter goes beyond Marxist understanding and expansion of the concept and hence constructs its own view with a Polanyian perspective based on morality and embeddedness issues. Similar to the first chapter's method, here also, conceptual exploration is supported with an empirical analysis wherein the extent to which Islamic finance contributes to financialisation of an economy is discussed in length. The empirical analysis evidenced that Islamic financialisation exacerbates the condition of overall financialisation in the economy, or alternatively, it fails to strengthen real economy through diluting financialisation trend.

Chapter 4 – *'Re-embedding Maqasid al-Shari'ah in the Essential Methodology of Islamic Economics'* – aims to explain why aspirations of Islamic economics and realities with Islamic financial practice contradict each other, and a divergence has emerged in consequence. Thus, this chapter attempts to pinpoint the knowledge creation methodology-oriented reasons for the observed failure whereby the importance of methodology in theory building and transforming knowledge into policy making is emphasized. *Maqasid al-Shari'ah*, therefore, is suggested as an essential methodology for Islamic economics and articulation of Islamic morality in everyday practice. In doing so, the prevailing view towards *maqasid* by modern scholars is criticised; instead a proactive *maqasid* understanding is constructed with its nine dimensions to stress the importance of methodology in the theorisation of Islamic economics. In this manner, the instrumentalised view of *maqasid* highly adopted amongst scholars of Islamic finance is seen as the root cause of mimicry and hybridisation within Islamic finance, which, as argued, should be replaced by policy oriented extended *maqasid* understanding.

CHAPTER 2

ISLAMIC BANKING AND DEVELOPMENT: REVISITING DEVELOPMENTALIST PROMISES OF ISLAMIC ECONOMICS

2.1. INTRODUCTION

The course of time evidences that the economic history of pre-modern societies embodies the 'moral economy' characteristic through which socioeconomic parameters, value systems and norms are embedded and preconditioned in the theoretical framework of an economy (*see*: Polanyi 1944). The embedment of morality in economic life and institutions allowed societal development to remain at the centre of economic relations and expedited the process of eliminating potential distortions among society through its masterminding role in all socioeconomic issues within a developmentalist perspective.

With the emergence of market economy, by contrast, economic institutions substantially gave way to modern forms in which morality is disembodied from the core of economic activities which ultimately bred a value free notion of economics. Along with the market economy, also due to the emergence of positive economic theory, the transformation from value loaded to value free character of economic settings are located; consequently, economic objectives were exposed to some contextual alterations in order to bring them into conformity with the new aspirations of 'positive economics'. In doing so, capital-intensive growth policies, nurtured by the Eurocentric[4] approach, superseded developmentalist policies implying a narrowing shift from normative to positive dealing of the concept of development. The issues of poverty, unemployment, wealth generation, equitable distribution of income and improvements in many spheres of public life, thereupon, have been tackled around this scant form of development.

As a result of dominance of market economy, the approach towards individual wellbeing, social welfare and prosperity is dealt, in the hegemonic economic thought, under the concept of 'economic growth'. Socioeconomic issues such as eradicating poverty, low economic

[4] Eurocentrism is a particular worldview that pursues European interests and benefits at the expense of the non-European world despite it claims to serve for universal beneficence (Mehmet 1999:10). It is the hallmark of Western economic development theorising in which capitalisation of almost everything is taken as the overriding objective in bringing material prosperity to the West.

performance, underdevelopment and inefficiency are all considered to be tackled as a result of economic growth. Adam Smith (1976) [originally published in 1776], one of the founding fathers of economics, emphasises the importance and scope of growth in his classical book '*An Inquiry into the Nature and Causes of the Wealth of Nations*' by stressing that the engine of growth is implicit in the division of labour, in the accumulation of capital, and in the technological progress. This materialist approach, notably spearheaded by capital accumulation with canonisation of GDP per capita, has penetrated every policy sphere of Eurocentric economic thought in dealing with developmentalist needs of individuals and societies. However, in practice, the inferiority of such growth policies, first implemented in the classical period, ended up with a great economic gap from which many countries, mostly those rooted in developing countries including the Muslim populated countries, have been suffering dramatically. The rationale for this growing inequality between countries as well as within countries has led to the reconsideration of the validity of mainstream economic theories and paved the way for the emergence of economic development or generally developmentalist theory and policy making.

Despite acknowledging the inferiority of conventional growth theories, especially after the Second World War, the fashioning of 'development' as a new phenomenon and prescription for underdeveloped nations could not go beyond becoming an unsophisticated extension of growth theories, for it failed to accommodate and endogenise societal, environmental, moral and humanitarian aspects –as well as the issues related to power allocation and income distribution. Consequently, economic development theories have remained to substantiate capital accumulation, leading to deepen the great competence amongst global powers to exploit world resources while it instrumentally included the fulfilment of basic needs of individuals as an objective. These theories, hence, could not respond to the question as to why some countries perform better than others and some cannot develop despite the fact that they use the same development strategies. Instead, the economic development theorising in the Western world has generated some development indicators such as Human Development Index, OECD Better Life Index, World Happiness Index, Genuine Progress Index, Inclusive Wealth Report, Global Sustainable Development Report, and Global Competitiveness Report to emphasise the difference in development trajectories by ranking countries accordingly. Although each index was expected to constitute a distinct alternative to growth-based indicators – mainly GDP per capita – and hence aimed to be a novel benchmark for the universal objective of developmentalism, they remained limited with particularistic approaches, far beyond reflecting multifaceted aspect of developmentalism.

In fact, the uniformity of Eurocentric theorisation of economic development with regard to its adoption to the same ontological and epistemological backdrop did not allow the proliferation of alternative views, which are distinct in their nature and fundamentally differ from conventional theories. It should, therefore, be recognised that questing intra-paradigm alternatives to mainstream theories cannot produce authentic solutions; hence, it is necessary to search for alternative economic development models and relevant strategies, which are substantiated beyond economics realm. This study, accordingly, suggests Islamic developmentalism, founded in the theoretical framework of Islamic moral economy, as an embedded form of establishing distributive justice that facilitates paradigmatic shift towards an authentic theory of development.

The emergence of Islamic economics in the post-colonial period in the modern times should be considered as a response to the overwhelming hegemony of market economy by embedding economy/economics and finance within the normative world of Islam and its value proposition. While in the initial discourse there were references to re-constructing the economic system of Islam by responding to the observed development failure in the Muslim world through the ontological construct of Islam, the main development out of this discourse has been the emergent pattern of Islamic banking and finance (IBF). In the initial consideration, IBF is considered to finance the economic development needs of Muslim societies within the imagined world of Islamic economics, the progress in the sector has demonstrated that it has not fulfilled the expectations yet as it has moved into conventional realm and operates within capital accumulation and financialisation terms. Therefore, in terms of transactional developments, Islamic finance and banking has been successful, while, as opposed to the expectation, it has failed to fulfil the developmentalist outcomes or transformational change in the Muslim societies. This study therefore aims at examining the impact of Islamic banking on development objectives beyond the essentialised economic growth objectives, as Islamic economics and economic development as an objective has withered away in the operations in the field as well as in academic research in the Muslim world.

2.1.1. Aims, Objectives and Research Questions

In an attempt to critically evaluate conventional notion of economic growth and development with the resultant imbalances it creates, the first essay aims to go beyond growth based economic theories and explores the economic development impact of Islamic banking through discursive and empirical analyses. It aims, hence, to unearth to what extent aspirations of Islamic economics match up with its practical outcomes, which essentialises developmentalism as an objective and Islamic financial institutions as institutionalised forms of epistemological knowledge.

In line with the stated aims, initially, a conceptual framework for Islamic developmentalism is constructed to identify the distinctions and dimensions of development, thereby, 'developmentalism' is brought out as the essential operational model of Islamic banking as envisaged in the emergence of Islamic economics and finance discourse. This is followed by an empirical analysis by employing a quantitative methodology through measuring and comparing performances of Islamic banks with an unbalanced panel of 21 cross section of countries observed during the period 2003-2014; thereby, it seeks potential contributions of Islamic banks on economic development trajectories of Muslim-dominated countries based on the predefined notion of 'Islamic developmentalism'. The underlying assumption, here, is that Islamic financial performance should not be confined to financial area only, as due to their moral construct they should be subjected to 'social evaluation' in the sense that Islamic moral economy locates Islamic banks as institutions of contributing to the social good or *ihsan*.

In relation to the aims and objectives, following research questions are developed:

RQ_1: Why does going through finance-growth nexus remain incapable in exploring the impact of finance on socioeconomic goals of countries?

RQ_2: What is the particular imagination of Islamic moral economy in relation to development paradigm?

RQ_3: In what ways does 'banking-development nexus' differ from 'banking-growth nexus'?

RQ_4: What are the most appropriate indicators accounting for Islamic banking growth and economic development?

RQ_5: To what extent does Islamic banking sector contribute to the developmentalist objectives in Muslim countries?

In overall, this study aims to provide a critical analysis as to why sole growth-oriented indicators for performance measurement of Islamic banks are inappropriate, mis-specified, dysfunctional and also inconsistent with IME's aspirational paradigm and hence with the realities of Muslim societies, which requires a value-oriented proposition. Therefore, it aims to bring out 'developmentalism' as the essential operational objectified model of Islamic banking, which was envisaged in the emergence of Islamic economics and finance discourse.

The rest of the chapter is organised as follows: Section 2 discusses, to a large extent, Islamic approach towards economic development with an overview of critically reviewing the accumulated literature in the mainstream developmentalist attempts. By locating the Islamic notion of development and its theoretical framework, Islamic social welfare institutions and their role on realising development throughout Muslim history are explained in detail. Whilst Section 3, delves into the role of finance in the conventional literature over economic growth performance, Section 4 and Section 5 render discursive and empirical evidence on the potential contributions of Islamic banking sector on economic development performances of countries.

2.2. ISLAM AND ECONOMIC DEVELOPMENT

As identified above as well as in Chapter 1, the emergence of Islamic economic movement is highly related with development objectives within the ideal objective of generating an economic system of Islam together with its economic development paradigm. In this, *Islamic financing*, as opposed to *Islamic financial*, is considered as an instrument to facilitate the development objectives by helping to mobilise resources for development. This is due to the fact that ‘Islamic financing’ corresponds to the everyday practice of finance surrounded by the principles and values of Islam, while ‘Islamic financial’ refers to a particular financial regime wherein finance has superior position in the economy with values and norms subordinated to the efficiency of the financial system (Asutay 2018). Therefore, it is important to understand the background of this emergence and the envisaged economic development nature of Islamic economics movement. This section aims at debating the development studies with an attempt to locate the Islamic economic development paradigm.

2.2.1. A Brief Survey of the Post-war Development Studies

The concept of development has been praised enthusiastically in the post-colonial period by leading exponents of Western progressive ideology as a way-out policy for newly independent nation states to disentangle from their ‘backward state’ in socioeconomic and political spheres. In line with this, development-oriented studies proliferated under a new modernist discourse known as ‘development economics’ with the motivation of crystalizing the roots of uneven development and its consequences resulting into social imbalance and inequality (Pieterse 2010).

Conceding that mainstream growth theory fails to reckon with wider implications of material prosperity such as distributional and welfare outcomes, and hence can only reflect “the shadow of real problems” (Hicks 1965:183), development economists emphasised multidimensional aspects of growth by claiming the possibility of multiple paths to achieve growth and development. It was admitted, therefore, that a universal theory of growth was nothing but a far-fetched illusionary idea in the sense of dressing up different bodies with a standard clothe. In line with this, Gerschenkron (1962:7), for instance, stressed that ideologies, policies and organisational structures of developing countries vary significantly; therefore, the scope of development policy based on industrialisation process should consider these factors to achieve success.

In light of the multidimensionality of development process, the interaction between developed and developing world is examined under two contrasting views of 'mutual benefit' and 'zero-sum game' (*see*: Singer 1952; Prebisch 1959; Hirschman 1981). The former approach emanates from Smith's seminal work of *The Theory of Moral Sentiments* (originally published in 1759). Accordingly, Smith [1759] (2010) argues that economic development and social change can be realised so long as individuals adopt moral values such as sense of duty, sympathy for others, self-love, cooperation and self-interest, and take them to the market as an enabling mechanism. This is expected to create a balance between self-interest and social interest, which, in return, would manifest the omnipotence of 'invisible hand'. In parallel with this, successors of this view claimed that there is a harmony of interest between advanced and developing countries, hence policy recommendations on how to develop and prosper for a developing country are mutually beneficial for both parties (for further details *see*: Hirschman 1981; Streeten 1985). Contrarily, zero-sum view suggests that there is a deeply-rooted conflict of interest in the development process of countries (Myrdal 1956:28) wherein comparatively advanced countries exacerbate the growing inequality under the guise of development policies recommended by international bodies (mostly Bretton Woods institutions) such as the liberation of international trade.

Criticisms towards the prevailing understanding of economic growth and development based on failed experiences, which later relegated and turned out to be statistical records, were signalling the emergence of a new discourse of 'alternative development' in the 1970s. No matter it be an intra-paradigmatic solution within mainstream economics, the continuous emphasis was, with one voice, on the need for structural change over economic systems of underdeveloped countries with a rationale of eradicating poverty, ameliorating income gap and help benefit the advantages of technological innovation. In doing so, a research programme was propagated mainly by World Bank, ILO and other international agencies to initiate 'basic needs strategy' as a developmentalist goal for both rural and urban economies, which puts heavy emphasis on the satisfaction of minimum human needs including health services, sheltering, supply of clean water and education, and essential public services with the efficient use of technology as the indicators of economic development (Evans 1976). However, it was recognized later that the application of structural change in an economy should go beyond basic needs strategy; instead, it hinges on political economy factors beyond Smithian understanding of natural harmony of interests argued under the 'invisible hand'. In other words, behind the retarding effects of development lie the conflicting interests of different stakeholders of society composed of privileged and disadvantaged groups (Olson 1982:55), which is in stark contrast to Smith's mythical view of the harmony between self-interest and social-interest.

The nature of interaction, either conflictual or mutually beneficial, gave way to the role of institutions on development process in 1980s with the rise of New Institutional Economics. Despite falling into structuralist position but in more sophisticated way, North (2003) criticized in general that the growth understanding of neoclassical economics based on the assumption of efficient markets does not account for differences in institutional structures amongst economies; hence, they fail to observe hindrances and de-incentivising motives to the development process caused by prohibitive institutional structures.

Similar to political economy approach but with a more micro level, Sen (1999) broadened the frontiers of development studies beyond structuralism and institutionalism through essentialising 'functioning' and 'capabilities' of individuals. In his view, development transcends the considerations of per capita GDP and institutional factors. Therefore, the objective with development should not be measured with 'being' of some goods sufficient in an economy, but rather 'having' it by stakeholders through enabling them to achieve its functioning (Sen 1999:190). Furthermore, human wellbeing or the quality of life cannot only be measured by observing the functioning individuals have. Beyond this, it is important to know what opportunities, freedom and advantages they could have achieved if their capabilities are enlarged. Sen (2003), thus treated development as 'capability expansion'. His views, then, inspired the emergence of 'human development' encapsulating education, health, poverty, and income inequality as the integral components of development.

The attempts to reveal a 'just' development process, surveyed above, uncloaked the importance of distributional issues. In this manner, in contradistinction to the utilitarian understanding that trusts on market mechanism to establish justice at the intersection point over which supply and demand meets, Rawls (1971) developed a counter argument under a social contract theory, wherein the assumption of 'veil of ignorance' paves the way for redistribution in the society with a free choice of individuals to constitute a rule of distribution.

2.2.2. Critical Approach towards Western Developmentalism and Its Applications

The evolution of the idea of post-war development within Western discourse unearths that the frontiers of growth understanding has to be expanded by re-examining developmentalist consequences of socioeconomic policies. However, it was recognised later that developmental articulations emerged out of the same epistemological knowledge failed to generate human-centred developmentalist policies. This is evident in the social and economic conditions of underdeveloped and developing countries together with challenging issues in the global environmental, health and educational areas that constitute a serious threat for future generations. It is hard, therefore, to claim that studies on development in the West paved the way for improvement in individual wellbeing and social welfare. Contrarily, development theories were constructed in such a way to fit into the historical progress, such as post-war experience, of advanced countries so that backward societies would follow their footsteps to reach the level of high development. In this sense, developmentalist prescriptions should be seen as a new way of organizing world politics to preserve nationalist interests. Otherwise, the long debate on development would show improvement in global equity and distributive justice as promised in discursive analyses.

A political economy approach towards the role of international institutions on development patterns of countries sheds light on the roots of developmentalist failure. It is argued, hence, that the experts at the World Bank, IMF and United Nations constitute the intelligentsia of development, and impose one correct answer against underdevelopment as free market ideology (Easterly 2009). Poverty, for instance, is relegated to a pure technological problem that can be overcome by the introduction of improvement in technical facilities, as projected for the underdeveloped African countries, such as improving communication technologies, efficient use of machines, breast-feeding education, and environmental friendly equipment, all of which neglect the hindering factors rooted in the domain of economics, sociology and politics (Easterly 2009).

On the practical side, when developmental policies, named as ‘structural adjustment programmes’, failed dramatically, the blame is put on mostly on the recipient countries’ structural imperfection, therefore development ideology itself has never been questioned. However, Western development project in the post-colonial period is in fact built on industrialisation process with pro-capital and technology intensive growth strategies. This meant that development has never been a universally applicable value-free notion, but rather at odds with the values of non-capitalist formation of societies due to a particular mode of production generated at the end. However, developing countries convinced that industrialisation, capital accumulation and technology are all transferable phenomena that have nothing to do with the existing social and economic formation. This view suggests that development can be achieved primarily through import-substitution, export promotion, technology transfer and foreign aid. Although the belief on development ideology still persists, it exacerbated economic problems in the last 30 years such as unemployment, inflation, stagnation, undernourishment, illiteracy, diseases, environmental threats, poverty, and distributive injustice in general.

Along with such destructive impacts, a new discourse has been attempted in the 1990s to respond multifarious dimensions of developmentalist failures caused by conventional policies and the underlying understanding. By essentialising sustainability in growth and development, some global goals related the spheres of earth's life, society and economy have been set up to constitute 'Sustainable Development Goals' (SDGs). One of the rationales behind SDGs mainly stems from the fact that short-run economic development strategies and policies successively pursued by developed nations in the post-war era turned out to result in developmentalist failure in the long-run due to the temporality of these achievements and temptation of short-run profit maximisation blurring the reality of slowing down of economy signalling a serious catastrophe in the future. In attempting to bridge the gap between short-run and long-run consequences of economic policies, SDG paradigm seems targeted mainly the relatively wealthy nations to reorganise the world ecosystem and social atmosphere in the light of global justice and humanitarian understanding (Kumar, Kumar, and Vivekadhish 2016; Sachs 2012). The active role was given to the rich countries, since the subject matter of development goals are settled to eradicate the economic catastrophes caused mainly by most capitalist societies. As the SDGs aim to gain a new approach towards world ecosystem, economy and society, it is hard to claim the existence of significant change in these areas. On the contrary, new issues have emerged rapidly, which widen the scope of threats.

2.2.3. Islamic Developmentalism

Islamic economics, as elaborated before, emerged to address the challenge of establishing an authentic development theory based on Islamic values and principles envisaged by Islamic system of economics so that the objective of distributive justice can be achieved. Founding fathers of Islamic economics, in this sense, invariably pondered upon the ways to realise Islamic developmentalism as a value-oriented activity in the modern era and hence made their contributions to eliminate the catastrophes of underdevelopment in Muslim regions. As the emergence of Islamic economics coincides with development crisis of Muslim world in the post-colonial era, an authentic developmentalist approach thrived as substantial alternative to the Western development theories and its failed applications over the poor parts of the world.

2.2.3.1. Theoretical framework

IME[5], one of the most critical to the conventional economic understanding, has shined out as a response to the so-called backwardness of Muslim societies with claiming its authentic nature, distinctive ontology and epistemology. Contrary to the market economy system, which confines itself with material development or economic growth due to its value or ethics free understanding, IME constructs development as a theory with the purpose of expanding human potential, functioning and capability in order to facilitate the ways to reach *falah* or human salvation in this world and the hereafter, which also constitute two-dimensional utility or *falah* function leading to society oriented *ihsani* function (or beneficence in the form of socialisation) in an Islamic framework. This approach necessitates a paradigm shift while pondering upon development issue so that Islamic development can articulate its multidimensionality by going beyond pure consideration of material aspects of social life through envisaging a harmony between spiritual, material and moral development as well as individual and social development (*see*, for instance, Ahmad 2000:17; Askari, Iqbal, and Mirakhor 2011:312; Chapra 2008; Siddiqi 2010). In its imagination, IME aims at re-defining factors of production, agencies, and institutions so that human, land, labour, capital and other stakeholders should be rescued from the 'exploitation' of the hegemonic systems to reach emancipation and empowerment aimed at Islam as a teaching and way of life.

The Islamic concept of development, hence, is considered to expand developmentalism and its practice into territories, which mainstream economics could not carry it into effect. For instance, Islamic developmentalism reveals, by nature, socioeconomic and socio-political change while needed. However, mainstream concept of development remains bounded with the cycle of quantitative category and unable to have substantial impact on such issues of justice, welfare, equity and peace. Accordingly, mainstream development strategy surrounded by capitalist interests misses the 'change factor' for individual, institutions and society, and the

[5] Before carrying the discussion forward, the distinction between IME and Islamic economics should be clarified. Since the term, economics, is already a neoclassical construct that has been subjected to serious backlashes by Islamic scholars, concatenating 'Islam' and 'economics' - as Islamic economics suggests - produces a conceptual inconsistency with Islamic teaching since Islamic economic model would seem otherwise as one of the variants of Western economics. Therefore, it is more convenient to use IME in responding to the aspirational system understanding of Islam with its aspirational proposition, as IME relates to an embedded system of economy rather than market dominance.

‘qualitative growth’ that is articulated through spiritual and moral aspects (Ghazali 1990). Thus, the Islamic vision discontents with growth alone and authenticates the concept of development with all its comprehensiveness and multifacetedness.

In concluding, this study recognises the value-loaded definition of ‘developmentalism’. However, it also recognises that IME’s aim is not only economic development but multi-faceted development within the parameters of *adalah, ihsan, rububiyah, khilafah and tazkiyah* in the context of *tawhidi* paradigm (Asutay 2013). Hence, developmentalism is redefined within Islamic normativeness by essentialising human-centred development through re-defining individual, as Islamic economics “aims at the study of human *falah* achieved by organising the resources of earth on the basis of cooperation and participation” (Khan 1984:55). In this context, re-defined developmentalism is objected towards emancipation and empowerment in every aspect of life within the *ihsani* social formation. In doing so, capital and its dominance is ‘de-centred’.

2.2.3.2. Axiomatic approach in constituting Islamic development

In developing the theoretical framework of Islamic economic development theory and paradigm, the axiomatic approach is helpful, since axioms constitute the parameters of theory construction. Axiomatic approach also helps to expand the operational aspects of Islamic developmentalism.

The first and foremost axiom of *Tawhid*, for instance, reflects complementarity and unitarity between material and moral aspects of individual life since both are considered integral to each other that avoid dichotomous improvement. In addition, everything in the universe is considered to be linked in a stakeholder manner; thereby, none of the stakeholders can be sacrificed in the name of development of others in the sense that the interest of each of the expanded stakeholders has to be sought. For example, environment or natural resources, in this manner, cannot be exploited with a rationale of profit maximisation in the economic sphere. Similarly, human, capital, labour and land have mutual contributions upon production process; hence, none of them should have superiority over others. *Tawhid*, in general, applies a moral filtering mechanism through its principles to preserve an equilibrium between different stakeholders’ rights observed in the relationship between individuals, individual-environment, individual-state, individual-society and individual-Allah. Thus, each of the stakeholders complements the other within unity. Consequently, at the core of Islamic economic development theory lies *tawhid*, as it arranges the political economy mechanism of development in terms of establishing the nature of the relationships between various stakeholders.

Following the *Tawhid* axiom, *al'adl wal iḥsan* (justice and beneficence) reflects the "horizontal dimension of equity" (Sirageldin and Anwar 1995:464). As Islam broadens and pinpoints the objectives of development through reckoning with the realm of *akhirah* or 'hereafter', individual development is redefined in terms of its success to reach *falah* (salvation) both in this world and *akhirah*. This view constitutes a great contrast with the idealised *homoeconomicus* individual prototype whose entire struggle is to maximise pleasure and minimize pain in this world. Therefore, human self-development can also be conceptualised as '*rushd*' or 'wisdom' process' (Askari, Iqbal, and Mirakhor 2014:317), which paves the way for making progress on the path towards perfection. Human beings, accordingly, is treated as ends, rather than means of development in human-centred development (Ghazali 1990). The understanding of human-centred development does not necessarily purport an adoption of humanist philosophy as essentialised in the Western perspective. The claim that man is at the hearth of development process and hence should be treated as ends rather than means should be understood in the context of *falah* and *ihsan*. In doing so, *ihsani* process necessitates the fulfilment of others' *falah*; thereby, individual centricity in development is an articulation of social development through *ihsan*. Therefore, an equilibrium function is attached to *ihsan* (Naqvi 1994), as those reached *falah* is expected to help to elevate the *falah* level of others who have not reached such a level. In other words, while self-development in the Islamic framework is accepted as an objective to fulfil, it has to be in harmony with social-development. In other words, individual *falah* should accompany with the establishment of *ihsan* (beneficence) in societal level. The internalisation of *ihsani* process eventually paves the way for Islamic developmentalism through articulating *al'adl wal ihsan* axiom. As can be inferred, two concepts *falah* and *ihsan* play a central role in revealing the nature and mechanism of development process.

A fundamental presumption of development process is related to the axiom of *rububiyyah* which is translated as divine arrangement for nourishment implying that Allah keeps providing continuously the ways and means of reaching perfection of both self and social development through divine guidance; as every creature is created with a potential of perfection. Therefore, social Darwinist explanations under 'survival of the fittest argument' (*see* for the discussion; Chapra 1992:30) give way to direct involvement and shaping of divine knowledge in the Islamic framework. As *rububiyah* axiom suggests that everything created with a developmentalist path to reach their perfection, and hence, it is the duty of the Islamic political economy to remove barriers preventing each stakeholder to reach to such level (Asutay 2018).

The emphasis on indivisibility of moral-material and self-social development is also reflected in the axiom of *tazkiyah,* which is described as 'purification plus growth'. This axiom clarifies that development is a process of purification of attitudes and relationships at the end of which all stakeholders in the universe are endowed with harmonious growth and gain mutual beneficence as contrast to zero-sum dealings of economic activities. In other words, as suggested by *tawhid*, each of the stakeholders' interests have to be considered in the development process as *fitrah* can only be achieved with balance through purification. For example, wealth has to be purified through returning the right of the society to society by paying *zakat*; and in the production process, for example, the right of the labour and environment has to be considered through the *tazkiyah* process so that the complementarity of *tawhid* should not be infringed.

Amanah (trust) and *khilafah* (viceregency), similarly, imply that everything in the universe is a trust from Allah given to individuals as trustees of Him, hence they have to be treated in the best way to reconstruct (*i'mar*) social environment through developmentalism. Individuals, as *khalifahs*, have a duty to transform epistemological knowledge of divine guidance in the form of developmental policy outcomes by involving as active agents of development process. This should bring social solidarity and unity amongst the society by ensuring moral dynamics embedded in the theoretical framework of economy.

The Islamic normative proposition, shaped by such axioms as the foundational and operational knowledge, aims at individual emancipation and empowerment for development at individual as well as societal level. Thus, a unique paradigm of developmentalism is suggested by IME, which questions the entire *status quo* for a fair, sharing, participatory and distributive economy in an embedded sense.

2.2.4. Social Welfare Institutions on the Way towards Islamic Development

The normative dimensions of Islamic development model based on its axiomatic framework had been institutionalised over the course of history. Muslim societies established authentic institutions to sustain social balance and improve welfare conditions of individuals. Therefore, Islamic developmentalism had always been practised by social welfare institutions, which produced social policies for individual self-development and social development in a stakeholder manner. However, these institutions emerged out of a demand from society and, to a large extent, were organised by civil society, rather than functioning as state apparatus to reallocate resources and redistribute income in favour of the privileged group with an active and central planning under the objectives of nation state. In this manner, shared values and norms had been embedded in these institutions' organisational framework in line with the aspirations of Islamic moral economy.

Although great number of institutions can be addressed here to exemplify the ways to realise Islamic development in Muslim societies, it is ample to mention only outstanding ones here. *Zakat* and *waqf* institutions, for instance, have mostly been referred in Islamic economics literature as examples of social development entities (*see*: Ahmed 2004; Chapra 2008; Kahf 1989, 2004; Siddiqi 2006; Mohieldin, Iqbal, Rostom, and Fu 2011; Sadeq 1996, amongst others). Whilst it constitutes micro foundations of developmentalism and encourages the wealthy to feel spiritually accountable for purifying their wealth, social development based on *zakat* had hardly been institutionalised and systematised throughout the history due to the difficulties in monitoring and organising the collection of *zakat* funds. Thus, the impact of *zakat* on formal economy has not been observed in a historical sense. However, notwithstanding this non-systematisation, *zakat* has a critical role on establishing redistributive justice by directly deterring the ambition of capital accumulation. As traditionally *zakat* accrues on idle money and therefore individuals are expected to channel their wealth in circulation within real sector, one of the wisdoms of *zakat* is to encourage active agents of Muslim entrepreneurs, investor, savers and consumers for circulation of their capital in the economy in order to generate value. Otherwise, capital accumulates in the few hands, and hence production process slows down. Income generation, later, hinges on alternative ways such as profit through interest-based system. The abolition of interest, similarly, can be considered as the rule that discourages people not to possess unfair profit through capital accumulation. Not only limited with this, *zakat* also encourages people to redistribute general wealth and contribute to social equilibrium by sharing certain amount of money with needy.

Awqaf institutions (*waqf* – singular), similarly, emerged from the demand for ensuring material, moral and spiritual development within society. As contrast to *zakat*, it had had macroeconomic implications and influence area over different aspects of social life. Mostly, it functioned as an institution for social policy making by active involvement of each stakeholder in the society over the process of Islamic development. It is important, here, to clarify that the era, in which *waqf* institutions were widely effective and considerably powerful, reflects pre-modern formation of societies. Thus, the omnipotent and all-encompassing modern state understanding was not present, as the primary role of state was on ensuring peace and security within its boundaries. This is evident in the Ottoman era in particular, since social policy making was extensively left to *waqf* institutions to deliver societal development (Kozak 1985). By keeping power in political sphere and preventing decentralisation of power, Ottoman sultans paved the way for social development through enabling *waqf* institutions. However, today, *waqf* is considered only to function as help and nurture the poor, provide sheltering for the homeless *etc.* (for a detailed role of *waqf* in the Muslim heritage, *see*: Boudjellal 2008; Cizakca 2000, 2002, 2011; Haneef, Pramanik, Mohammed, Dahiru, and Amin 2013; Kozak 1985; Kuran 2001; Mohsin *et al.* 2016; Zuki 2012). It should also be noted that *waqf* system is heavily romanticised in relation to its past history; as *awqaf* were available mainly in the main cities as well as capital cities around the power house of sultans, while Muslim periphery did not have access to the richness of *awqaf* system. However, this does not negate the positive impact of *awqaf* system within the larger environment they operated, neither this denies the enormous potential role it has in responding to the current poverty and underdevelopment in the Muslim world.

In addition to *zakat* and *waqf* institutions, there are some other prominent institutional forms of knowledge that articulate Islamic developmentalism in the history. Amongst them, 'crafts and guilds organisation in the Ottoman empire' (Faroqhi 2009; Inalcik 1969; Islamoğlu and Keyder 1977; Lewis 1937) had reorganised society in fulfilling development in the economic realm. Mainly composed of three fields as agriculture, economic transactions in urban and rural areas, and general trade, economic activities in the Ottoman society were more or less controlled and organised by the crafts and guilds organisation to prevent unfair competition and capital accumulation in the few people's hand. This way of organising society and economic sphere forestalls leaving individual in the market alone; on the contrary, each member of these organisations had relative power during the competition in the market. Thus, harmonious growth, or *tazkiyah*, was established by thinking of economic activity as collective action.

Hisbah institution, in the medieval Islamic era, played another major role on regulating market in the light of developmentalist objectives (Islahi 2006; Khan 1982; Lewis 2005; Oran 2010). Mainly based on the notion of enjoining the good and forbidding the evil, *hisbah* institutions aimed to establish social justice within market playground.

Lastly, the institution of *akhi* organisation (*akhism*-Islamic brotherhood) in Ottoman period can be mentioned as another example of social welfare institutions in Muslim history, which were practised between the 13th and 20th century with the aim of establishing professional ethics in business environment through cooperation, solidarity, tolerance and integrity (Çaha and Karaman 2006; Güneş and Güneş 2012; Şahin, Öztürk, and Ünalmış 2009) in an embedded manner by having business, religious practice, religious education and apprenticeship to develop an embedded society in the moral norms of Islam.

As evident in the history, Islamic development had always been a central issue in both society and state level. In responding to fulfilling social and economic development, a large number of institutions, dissected in length above, were established. Modern period, especially the 20th century, gave birth to Islamic finance idealised as authentic form of developmentalist institution that responds to underprivileged situation of Muslim nation states. The following sections discuss, to a large extent, the normative dimensions of the emergence, ascendance and role of Islamic banking and finance over the development trajectories of countries.

2.2.5. Islamic Finance and Development

The multifaceted phenomenon of development had always been a central concern for individual, society and state during the course of time in different eras. Muslim societies, in this manner, responded to developmentalist needs by establishing authentic institutions as elaborated in the previous section. The substantially changing politico-economic environment in the modern period, however, complicated the emergence of such institutions and hence obstructed the flourishing of alternative institutions that would play a pivotal role in constituting social justice and welfare by essentialising *falah* and *ihsan* oriented development project.

Since the traditional institutions could not bring into compliance with modern social formation of Muslim societies, Islamic banks and financial institutions have emerged and have been established and popularised as a value-oriented financial proposition that aims to facilitate paradigmatic shift against the overwhelmingly hegemonic character of self-regulated market economy understanding. Whilst market economy foundations and its global impositions inhibit development process in Muslim lands through creating tension between human well-being, land, labour and money that results in social injustice, Islamic finance is believed to partake in endogenising humanitarian, social, economic, environmental and moral aspects of Islamic developmentalism. Thus, rather than transactional development, IBF institutions were initially envisaged to bring about transformational development so that paradigmatic change towards an Islamic system of economy can be established.

The role of Islamic finance over the idealised transformational development, which does not only hinge on the success of IBF but also requires other institutional contributions, was shaped to ameliorate distributive justice through enhancing power and resource allocation leading to wealth distribution, respectively, in the society, and to develop capabilities and functioning of individuals through capability expansion. In the light of this, Islamic finance, in an aspirational sense, is equated with social impact finance, and hence, its social performance was prioritised over financial performance. For this reason, the experiences with Mit Ghamr and Tabung Haji (explained in following sections), have always been yearned and commemorated to improve Islamic financial industry performance since its inception.

The aspirations with Islamic finance necessarily break the traditional boundaries of financing, such that conventional finance with its intermediation role was replaced with the idea of considering Islamic finance as business model (this issue is explained in section 2.4). This is due to the fact that the asset backed, and equity-based nature of Islamic finance completely differentiate its operational structure from conventional financial system, which, therefore, no longer pursues mere financial intermediation but directly takes share in value-adding in real economy. Based on such features, Islamic finance aimed to constitute an embedded institutional form of participatory economy through essentialising the idea of 'development with sharing'.

The development and capacity building propensity of IBF proposition is related to redefinition of capital and its ownership. As explained by Asutay (2018), according to the *tawhidi* paradigm, the prohibition of *riba* aims to determine a new modes of production within Islamic social formation, in which the dominance and hegemony of capital is removed; instead, capital is treated equal with the rest of the stakeholders. This, hence, creates opportunity space for other stakeholders to flourish, emancipate and empower through providing equal opportunities (*see*: Asutay 2017); and hence the entire process aims at multidimensional development. Therefore, Islamic political economy features profit and loss sharing and risk sharing in the form of equity financing in shaping Islamic finance as the main thrust of expanding stakeholder for development by providing accessibility to resources (Asutay 2013).

The essentialisation of profit-loss sharing and risk sharing principles of Islamic finance is highly associated with two important legal maxims of (i) 'gaining is by accountability' (*al-ghunm bi al-ghurm*) and (ii) 'income is bound by assured obligation' (*al-kharaj bil-daman*) (*see*: Ahmed *et al*. 2015:12; El-Din 2013:147). These two legal maxims are derived from the

Prophetic *ahadith* the former is derived from the *hadith*[6] that: “A pledge should not be blocked from the one who provided it, as the provider deserves gaining (*ghunm*) from it and bears accountability (*ghurm*) towards it”. The second maxim, *al-kharaj bi al-daman*, is derived from a hadith[7] of the Prophet implying that “if the borrower of money or any fungible good (for instance, rice, wheat or cement) deserves the income (that is, the *kharaj*) generated from the loan in whatever form (for instance, productive growth, trade profit and food) against the assured obligation (the *daman*) to pay back the loan to the lender” (El-Din 2013:147). Accordingly, in every Islamic financial contract, the entitlement of gain must incorporate responsibility, and financial return has to accompany certain degree of risk. This necessarily requires the adoption of sharing principle in generating profit or bearing some risk and loss. Such principles of IBF are also expected to produce a participatory society in general, which is again an essential part of the Islamic political economy’s imagination of development, as individual emancipation and development can only take place in a participatory society in which stakeholding through development is extended as substantiated by the *tawhid* axiom in the sense of complementarity.

As part of the participatory financing in the form of profit-and-loss sharing and risk sharing, in fulfilling the institutional logic of IME and its modes of production, IBF institutions are expected to concentrate more on partnership-based instruments (such as *mudarabah* and *musharakah*) as opposed to constituting debt-based financing model with of Islamic metaphors and methods in modern period (mainly *murabahah* and *tawarruq*) with an aim of minimising (or even removing in some contracts) risk and profit and loss sharing, which is required by the capitalist institutional logic.

Although the modern *fiqhi* positioning has no reservations on the use of debt-based Islamic financial instruments, IME understanding evaluates these instruments according to their potential contributions and consequences in relation to the real economy through generating value-added. In this sense, *murabahah* can be considered as permissible in the *fiqhi* area by arguing that the basic framework in the transactions is *ibahah* or permissibility, but the consequentialist approach necessarily discourages any debt-based instrument that gives rise to unproductive economic outcomes by exacerbating indebtedness in the society. It is also important to distinguish debt-based modes of financing as *fiqh* structure in a historical sense as opposed to the debt-based financialised economy. The constitution of *fiqh* in a histrocial sense

[6] Ministry of Awqaf and Islamic Affairs (1994), *Al-Mawsu’a Al-Fiqhiyyah*, vol. 19., p. 259.
[7] Ministry of Awqaf and Islamic Affairs (1994), *Al-Mawsu’a Al-Fiqhiyyah*, vol. 19., p. 261.

refers to debt-based transactions used as part of the business model, while in the modern times the use of *fiqh* in referring to debt-based modes relates to financialised economy, which had not been the reference point of *fiqh* in its historical formation.

IME also shapes Islamic financing in the form of real economy related financing to ensure embeddedness; and therefore, financing is constructed through instruments which essentialises asset-backed structures. In line with this, therefore, fictitious commodities and their financing is not considered which aims to prevent the emergence of toxic financing instruments that prevails in the conventional finance. Real asset-backed financing is an essential part of Islamic development in terms of extending stakeholding and capacity building as well as developing productive economy which can help job creation (Asutay 2013, 2018). In line with this, financial markets are not essentialised as investment areas, since they do not represent real economy.

The emergence of Islamic capital markets such as sukuk is also considered as an important resource mobilisation for infrastructural development leading socio-economic development (*see*: Bacha and Mirakhor 2013). The recent debate on green sukuk as well as infrastructure financing should be considered as important aspects of development-oriented financing aspect of Islamic finance.

In line with this, IBF is expected to direct its resources to value creation oriented economic activity in real economy, socially beneficial investment, infrastructure financing, financing education, research and development which can address global concerns in relation to developments in the form of environmental, social and governance (ESG), sustainable development goals (SDGs), corporate governance and corporate social responsibility (CSR) (*see*: Ahmed, Mohieldin, Verbeek, and Aboulmagd 2015).

An important micro dimension of Islamic finance being development oriented is financial inclusion which is also an essential thrust of SDG paradigm. Islamic finance aims to overcome financial exclusion due to religious choices such as Muslims being excluded from the conventional financial system due to *ribawi* transactions. The expansion of IBF has provided an opportunity for individual Muslims to have access to *riba-free* and *Shari'ah* compliant financing for financial inclusion (Iqbal and Mirakhor 2013b). However, as Asutay (2014) argues, Islamic finance aims to go beyond simple 'bank account holding' oriented financial inclusion; but rather Islamic finance, as part of IME, aims to empower individual for capacity building through financial inclusion so that development of individual and society should be achieved. Therefore, it is suggested that Islamic finance should consider expanding into micro-finance and crowdfunding as well as SMEs financing areas to enhance capacity building oriented nature of Islamic finance by essentialising equity-based financing options including, but not limited to, *mudarabah*, *musharakah*, *qard al-hassan*.

Another important dimension of Islamic finance is its link with the traditional social welfare institutions. In other words, the normative dimensions of Islamic finance were envisaged extensively to address individual and social development in the modern period, that was once, achieved by traditional institutions including *waqf* and *zakat*. With the burgeoning of IBF, traditional institutions such as *zakat* and *waqf*, has found new opportunity spaces for expanding their contribution for social welfare of Muslim societies; as it has been now possible to bring the properties owned by *waqf* is a profitable environment through Islamic financing so that further social activities can be undertaken (Karim 2010). In addition, with developing financing understanding, *zakat* funds have been developed beyond *zakat* giving so that capacity building can be expanded for development to take place in Muslim societies.

Apart from the direct implications of the distinguishing features of Islamic finance within the financial sphere, it can ideally generate social implications and wider articulations. Therefore, the existence and considerable share of Islamic banking in a certain economy necessarily address the distributional issues of income inequality, poverty alleviation and reducing unemployment through, for instance, *zakat* and *awqaf* funds (Ahmed 2004b; Chapra 2009; Cizakca 1998). Likewise, unemployment can be reduced by generating self-employment opportunities through SME financing, *qard hasan* funds and microfinance (Abdul Rahman 2007; Ahmed 2004a; Aysan, Disli, Ng, and Ozturk 2016; Huda 2012; Mohieldin *et al.* 2011; Wilson 2007).

As the global era imposes on the advancement in technological area, Islamic banks can lead the promotion of education, research and development activities in different fields including technology as observed in Islamic Development Bank. Islamic developmentalism can also be articulated in the bank level through authenticating and reconceptualising environmental, social and governance criteria (ESG) or sustainable development goals (SDGs) through Islamic values. Based on these features, Islamic banks can be an embedded part of development process by mainly functioning as participatory and responsible finance together with the understanding of community banking, which "serve to community not markets" (Asutay 2007b:8).

In sum, IME considers financing as a facilitator for development, as "finance is not about 'making money' per se. It is a 'functional' science in that it exists to support other goals – those of the society. The better aligned a society's financial institutions are with its goals and ideals, the stronger and more successful the society will be" (Shiller 2012:7). As part of the same wisdom, Islamic worldview aims to develop individual and society in line with the axioms identified; and considers Islamic finance as one of the instruments for such a purpose.

The authenticity and aspirational facets of Islamic finance, however, could hardly be accommodated in the practical field (due to many reasons explained in great detail in Chapter 3. The prevailing understanding of market economy permeated through Islamic financial sphere and normativeness has been sacrificed at the expense of profit maximisation and efficiency orientation. Thus, expectations on fulfilling developmentalist objectives gave way to sacralisation of economic growth through the essentialisation and expansion of financial markets, which is discussed in a later section in this chapter as well as in the following chapters.

2.3. LITERATURE REVIEW ON FINANCE, ECONOMIC GROWTH AND POLITICAL ECONOMY: LOCATING THE GAP

An intensive debate on finance-growth nexus corresponds to the 19th century in economic history when finance proclaimed its independence and superiority from 'economy' through a heavy financialisation of economic institutions, which engendered a substantial rearrangement in political, economic and social relations. Such a transformed paradigm in relation to the pre-modern moral economy paved the way for stimulating discussions about impacts of finance on economic growth. As consequences of these discussions, following issues have been raised exhaustively by many scholars since then:

(i) indicators of financial development and economic growth;
(ii) the role of financial institutional bodies on economic growth;
(iii) causality and linearity-nonlinearity issues between financial development and economic growth;
(iv) noneconomic parameters including institutional and legal environment encompassing finance-growth nexus; and
(v) the role of financial liberalisation and financial repression policies on the nexus.

In understanding the orientation of the debate in finance-growth nexus, a selection of seminal empirical studies of the last five decades related to finance-growth nexus are tabulated in the appendix (*see* from Table A.2.1 to Table A.2.6). These studies are classified expressing particular focus areas and the key findings develop in this study. In reviewing empirical part of the literature, these tables are referenced and evidenced in order to shed light on the debate. Theoretical discussions on finance-growth nexus in the existing literature, on the other hand, are introduced and explained in detail in the next section.

2.3.1. Economic Factors

A highly-intensified debate on finance-growth nexus has given rise to two opposite views about the role of finance over economic growth. Schumpeter (1911), as an early contributor to the debate, argued that sophisticated financial systems could breed technological improvement, increase productive capacity and, hence promote economic growth. In addition to this, Schumpeter (1911) specifically underlined the need for credit markets in providing credit for entrepreneurs' investment projects and in facilitating their adaptation to technological improvements through attaching a critical role to banks about the intermediation of financial operations. Robinson (1952), responding to this, proposes a counter argument by favouring finance in promoting economic growth wherein he understates functions of financial institutions by attributing them a passive role and, further, equates financial development (henceforth FD), with one of the necessary outcomes of rapid industrialisation. He maintains, with his assertion, that economic growth requires finance because of a simple need; that is to meet the demand in the market (Robinson 1952). This view implicitly emphasises a reverse direction about the link between FD and economic growth by centring growth into the core while placing FD as necessary process and outcome of growth effect.

After the World War II, studies on finance-growth nexus contrasted on two prominent views together with the contributions of Schumpeter (1911) and Robinson (1952). Financial repressionist view, based on theoretical studies of Keynes (1937) and Tobin (1965), advocates the need for government interference in financial system and control on credit market through "interest rate ceilings, high reserve requirements and directed credit programmes" (Demetriades and Andrianova 2004:49). By doing this, it is believed that "financial repression reduces the demand for money in favour of productive capital, thus raising the capital/labour ratio and accelerating economic growth" (Eschenbach 2004:6). In their empirical study, Demetriades and Luintel (2001) find evidence that financial repression in South Korea positively affected its FD leading to economic growth. However, as most empirical studies evidence, repressionist approach makes holding money less profitable and credit less available for investors. Eventually, banking system together with other financial institutions became dysfunctional and ineffective in fuelling economic growth within this approach.

Consistent with the Schumpeterian line, financial liberalisation view has advanced by some many contenders including Gurley and Shaw (1955), Goldsmith (1969), Hicks (1969), McKinnon (1973) and Shaw (1973) in response to the Keynesian idea of financial repression. The main contributions of these contenders are that financial repression policies should be challenged by allowing interest rates to act freely and abandoning high reserve ratios and decontrolling government interventions, since they all impair the dynamics of growth through immobilisation of savings, inefficient allocation of resources and technological inertia. Goldsmith (1969) was the first contributor who conducted a meritorious econometric study on finance-growth nexus with a cross-section analysis wherein is deduced that size and efficiency factors in investments make significant contributions to economic growth. On the other hand, McKinnon (1973) contends, with his 'complementarity hypothesis', that investment can be materialised as long as banks hold enough saving accounts, while Shaw (1973), with his theory of 'debt intermediation', contributes to the debate by stressing the role of borrowing and lending as an instrument for increasing investment and output.

1980s accompanied with neoclassical critical to McKinnon-Shaw model of financial liberalisation. Stiglitz (1989), for example, advocated some impairing aspects of financial liberalisation upon economic growth with exemplifying market failures resulted by free credit markets. Stiglitz (2000) also adds that periodical financial crises are in high correlation with the liberalisation of countries' financial systems. Taylor (1983) and Van Wijnbergen (1983), on the other hand, asserted that financial liberalisation policies are less likely to foster economic growth when there are efficient working curb markets (non-institutional credit markets) in the market. The role of government, among critics, was stressed by Mankiw (1986) who supported government intervention in order to alleviate market failures through regulating credit allocation.

Emerging in 1990s, the endogenous growth model theoreticians re-criticised McKinnon-Shaw model by claiming that financial intermediation should not target maximisation of the volume of investment primarily, but rather it must prioritise the attainment of efficiency. Further, endogenous models highlight that finance and growth exhibit binary relationship in which these two reciprocate each other (Ang 2008:542). By the same token, Greenwood and Jovanovic (1990) emphasised this bidirectional relationship by asserting that financial institutions eliminate the informational problems and risks related to them, thereby allowing for growth; while growth, in turn, prepares necessary instruments in order to create efficient financial structures.

The adaptation of liberal financial policies in economic institutions, ultimately, brought about a debacle, especially on developing countries in 1990s. This led the contenders in the field to modify their premises about favouring financial liberalisation without taking country specific factors into account. Within the new approach, it is asserted that formation of a proper regulatory framework is indispensable within financial liberalisation in order to foresee and avoid potential financial crisis (De Gregorio and Guidotti 1995; Stiglitz 2000). However overall, a gradual financial liberalisation through correct sequencing of reforms (McKinnon 1991) was seen a remedy in overcoming the detrimental effects of financial liberalisation (Demirgüç-Kunt and Maksimovic 1998).

An authentic debate, in the last twenty years, has set in to compare market based and bank based financial systems (*see*: Allen and Gale 2000; Chakraborty and Ray 2006; Demirgüç-Kunt and Levine 2001; Levine 2002; Uzunkaya 2012). It can easily be observed that a bank based financial system is more widespread in developing countries, where banks, within their monitoring role, have primary functions of allocating resources and providing finance to firms which have very few shareholders with large stakes. A market based financial system, on the other hand, is less dependent to the banking sector with regard to fund allocation (Khan and Senhadji 2003:92; Rajan and Zingales 2003:12), as in such environment financial markets are found to be dominant over fund allocation process. In financially developed countries, such as the USA and the UK, financial system is consisted of large number of shareholders with relatively small stakes. In close relation to this debate, effects of stock markets, beyond a bank based financial system, are considered whether it supports economic growth within a market based financial system. Keynes (1937) criticised stock markets in their role on delivering economic growth and stated that the existence of stock market produces too much speculation which eventually results with destabilisation of economy. Similarly, but more fundamentally, Singh (1997) and Harris (1997) argued that stock markets in developing countries inhibit economic growth since financial sector in these countries suffer from informational problems dramatically and, hence, it leads to create more fragile markets. Therefore, in general, efficiency of stock markets hinges on an environment where informational asymmetries are at minimum level, stock prices are not volatile, and prices are stable, as they cannot be easily manipulated. The economy, having these features, reveals more powerful financial system with stock markets (Arestis, Demetriades, and Luintel 2001).

2.3.2. Multidimensional Factors

Investigating a relationship between two or more variables thoroughly requires multidimensional approach in order to capture multiple impacts amongst each variable. In the same manner, comprehensive evaluation of a particular study in certain field necessitates looking from a broad perspective which also incorporates other factors into analysis. Thus, causes or leading factors of a certain phenomenon should be sought within such a wider context. In the case of FD-economic growth nexus, if determinants of FD, its interaction with economic growth or driving forces of growth are narrowed by considering them a mere financial issue through abstraction of other factors from the analysis, then problem detection and possible prescriptions cannot be addressed in a right way. In order to evade such an outcome, FD should not be confined to economic explanations, but rather it must be associated primarily with politics and history (Morck and Steier 2005:50), as economic and financial events are also affected by larger political, social, legal and anthropological factors. Thus, a political economy perspective on FD-growth nexus can help to expand the explanatory power of any economic model. This section, therefore, aims to discuss such factors affecting FD and economic growth nexus.

2.3.2.1. Political economy factors

The way of political actors' involvement in economic decision-making process has significantly evolved during the last decades. Notably with the contributions of public choice, it is no longer considered that policy makers undertake the role of 'benevolent social planners' because their political incentives stimulate them to act as 'self-interested agents' (Pagano and Volpin 2001:503). As such, choices of political and financial powers – both are interest groups acting in concert to exert their power over economic and political institutions - move away from that of the dispersed groups in the economic system which results in favour of the former group. Therefore, one of the important reasons for economic underdevelopment addresses the transformation of the role of policy makers. Along with this, Rajan and Zingales (2003) stress political factors with its potential benefits; the idea that enhancing FD in an economy can induce and facilitate economic growth. Through such a lens, they introduce 'an interest group theory of financial development' which emphasises two interest groups directing an economy's financial system into a certain structure. In this approach, there are two distinct groups: 'financial incumbents' and 'industrial incumbents' who resist FD through hampering financial liberalisation and openness of an economy, since it is believed that FD accompanies with competition which, then, threatens the prevalence and power of these incumbents in a financial system.

Industrial incumbents, in such a financial system, have privileged position in reaching financial opportunities, so they seize the biggest portion of financial sector. Without any permission and implicit approval of industrial incumbents, it is not possible to have a position or make large-scale businesses in the financial system. Similar to this, financial incumbents form 'relationship-based' financing where cartel financiers construct a network/relationship within those who have penetration upon firms, thereby they get firm-specific information through informal ways and compel firms to get finance from these cartels. As a result, they subjugate financial sector and become monopolies in the economy (Rajan and Zingales 2003:18).

In an economic system within the existence of these incumbents, FD becomes possible "only when the country's political structure changes dramatically, or when the incumbents want development to take place" (Rajan and Zingales 2003:21). However, more fundamental solution to cease the prevalence of the incumbents in a financial system, according to Rajan and Zingales (2003:18), is to allow capital flows, international trade and developing "better disclosure rules and enforcement".

Together with the contributions of Rajan and Zingales (2003), the role of 'political incumbents' in delivering economic growth through proper FD process should also be included into the analysis. In this sight, political incumbents engross whole financial sector by exerting their parliamentary power or by derivation of laws in line with their interests. Subjugation of the financial sector, then, requires existence of a special elite class to which a certain portion of the surplus is distributed as a result of their interest pool with the political incumbents. This kind of environment, however, breeds a system where a minority group unproductively and inefficiently operates financial sector, which necessarily eventuates economic underdevelopment.

A critical approach to the works of Rajan and Zingales (2003) can be raised through examining the role of global incumbents on FD and growth. This way of thinking comes up with the idea that a minority interest group has significant dominance upon global financial sector through enjoying large shares. These players are closely involved in the decisions about financial markets and use their global financial institutions (MNCs *etc*.) to control capital flows in underdeveloped and developing countries. Therefore, these countries are not able to get economic freedom to achieve sound financial systems as long as their financial systems are exposed to global financial powers' exploitation. Resultantly, financial liberalisation and openness as part of FD policy, contrary to Rajan and Zingales (2003), might not lead to economic growth.

Beside the work of Rajan and Zingales (2003), the role of politics in achieving FD and sustainable economic growth is also addressed by Haber (2002) from a different angle. He underlines that economic activities must be approached within impact of political institutions upon them rather than envisaging an insulated market understanding, which assumes no involvement of noneconomic factors in market activities. Based on this line, it can be said that the presence of competitive markets with regard to the satisfaction of requirements for strong financial systems and for robust growth policies can only exist in an environment where there is an effective working political competition. Otherwise, financial modernisation would be prevented by the entrenched political powers through, for instance, inappropriate regulative policies of governments which lead banking system to work inefficiently (Haber 2002:39).

Institutions as dynamic factors for FD and economic growth should be given much emphasis since there is a general misunderstanding about the causes of economic growth which sees capital accumulation, technology, education and other factors as the underlying causes of economic growth. However, in fact, they should be considered as the reflections of growth, not the true causes of it. The leading factors and explanations of FD and growth, indeed, have to be sought in the structure of institutions, which influences whole economic activities in a given society (North and Thomas 1973:2). By acknowledging this, it can be stated that different institutional structuring in an economy elucidates rationale for the existing dissimilarity of growth performances among countries, and it also allows for the acquirement of advancing growth levels. Financial institutions, in the light of this explanation, exhibit a catalyst role to achieve this advancement.

A general enquiry as to which type of political regime supports FD and fosters economic growth in a best way is, generally, associated with democratic and authoritarian regimes. Some contenders, including North (1990) and Olson (1991), approach to the debate from the point of property rights, which is believed to be a strong cursor for economic growth, and they conclude that democratic regimes, by their very nature, protect property rights stronger than other regimes.[8] In line with this, democratic systems have great potentials to eliminate substantial problems stemming from dictatorial or authoritarian rulings. For instance, the existence of

[8] Przeworski and Limongi (1993:52) oppose to this assertion and argue that "the idea that democracy protects property rights is a recent invention, and we think a far-fetched one".

transparent institutions and the attitude of disclosing political and economic activities in democratic governments help fundamentally to minimise corruption in the society. In contrast to democratic view, some other scholars (*such as*: de Schweinitz Jr 1959; Galenson 1959; Rao 1984) argue that democratic systems compel individuals to consume more and save less which, then, leads to decreased investment activities and hence slows down FD. In response to the second view, Przeworski and Limongi (1993:56) suggest that there must be some isolated institutions in order to evade and resist such an implicit exploitation, and give the example of Asian states by stating that "the key to the superior economic performance of the Asian 'tigers' is 'state autonomy,' defined as a combination of the 'capacity' of the state to pursue developmentalist policies with its 'insulation' from particularistic pressures, particularly those originating from large firms or unions". Within a similar approach, Kurth (1979) is explicitly eager to justify dictatorship solution against democratic alternatives with regard to its facilitation of economic growth through restraining power of labour unions and moderating wages. Durham (1999), contrary to popular belief, utilises from Gerschenkron's (1962) thoughts[9] by stating that poor economies can grow faster than more advanced countries which, in turn, puts authoritarian governments of backward countries at the core of rapid industrialisation process, since "the greater the initial backwardness, the greater the required state intervention necessary to affect industrialisation" (Durham 1999:82).

In general, however, scholars agree on the idea that state autonomy can easily transform to the dictatorship model which always tends to result in inefficient solutions and does not distribute resources smoothly whereas democratic regimes are supposed to serve for the general interest through providing a participatory environment.

2.3.2.2. Legal and societal factors

Differences in legal systems provide another standpoint for the explanation of FD and economic growth interaction. Other than economic variables, legal structures of countries can also establish a ground for sound financial systems and robust economic growth. Pertaining to this, Porta, Lopez-de-Silanes, Shleifer, and Vishny (1998), aimed in their seminal study to explore the effect of common law and civil law on financial performance of countries. In terms of providing legal protection to shareholders, private investors and external entrepreneurs, La Porta, Lopez-de-Silanes, Shleifer, and Vishny (1998) asserted that common-law countries are

[9] Gerschenkron (1962:8), far from traditional approach, states that economically backward countries are more advantageous than other countries in performing faster growth since they embody cheap labour, 'greater backlog of technological innovations' and 'borrowed technology' which allow for quick industrialisation.

respectively more successful than civil-law countries, as common-law generates an opportunity space for development beyond the codification of civil law. Further, legal sanctions were observed to be stronger in the common-law countries as well. These imply that a financial system with a strong legal system, which safeguards all financial agents against any kind of illegal circumstances through protecting their property rights, can complete its FD process efficiently and hence foster economic growth.

In the relevant literature, it is argued that efficient working financial regulations, as associated with legal systems, primarily strengthens banking system of an economy and paves the way for growth-leading capital market liberalisation (Pagano and Volpin 2001; Stiglitz 2000). The positive role of financial regulation is conceptualised by Kroszner (2000) as ‘the public interest theory of regulation’. This view suggests that regulations in financial and banking sector help to alleviate market failures and protect those consumers who suffer from information asymmetries, then ultimately lead to maximise social welfare (Kroszner 2000:26). Notwithstanding this, regulatory structures are also exposed to political pressure groups’ and lobbying groups’ manipulations which can be explained by ‘the private interest theory of regulation’ (Kroszner 2000), wherein the two groups aim to retard financial reforms because the existing regulatory framework is constructed in favour of them (Pagano and Volpin 2001:517). Deregulation policies, by the same token, are considered by those groups as deviations which undermine their financial interests through creating more competitive environment (Kroszner and Strahan 1999:1444). FD, thus, cannot be carried out in such an environment where recently mentioned incumbents control regulatory bodies and designate the content of regulatory structure.

Corporate governance is, in a similar manner, an important dimension of the finance-growth nexus. If the power between stakeholders (shareholders, managers and employees) can be balanced and governed in a fair manner by companies, a cooperative environment exists in that company which, then, contributes to FD process of an economy positively (*see*: Kraakman and Hansmann 2000; Pagano and Volpin 2005; Roe 1994; Tirole 2001). Otherwise, managers would tend to preserve shareholders’ interests only and do not put much concern for the rest of stakeholders’ interests. A stakeholder model has, thus, strong connections with the legal origins of countries. Specifically, if a legal system protects every stakeholder’s rights through relevant laws and encourages them to participate in corporate governance, financial system can, then, be further strengthened. In this, political power is considered to be a key, since they create corporate structures through legislating laws about protection of rights.

Beside the pervasive effects of diverse legal systems on FD-growth nexus, societal factors, more precisely cultural factors, should not be underestimated in supporting this nexus, and they should be regarded as complements to legal factors. The fact that values and norms shape economic behaviours of individuals in their everyday life, including their financial activities, implies that societal factors derived from these values and norms have an indirect decisive role on the FD and economic growth process. For instance, 'trust' can be a key factor for alleviating problems pertaining to FD, which are not, at the same time, possible to be coped with by legal institutions (*see*: Guiso, Sapienza, and Zingales 2004; Inglehart, Basanez, and Moreno 1998; Knack and Keefer 1997). Similarly, societal norms as informal institutions can trigger stock market development through shareholder protection and lead to accelerate economic growth through banking development and protecting creditors' rights (Garretsen, Lensink, and Sterken 2004:173). To demonstrate this, Garretsen, Lensink, and Sterken (2004) conducted an econometric analysis in which they derived societal indicators by utilising Hofstede's work (1980) in order to explore the effects of societal factors on FD and economic growth and compared the outcome with the work of Porta Lopez-de-Silanes, Shleifer, and Vishny (1997) who searched for the effects of legal factors on FD.

After elaborating on the societal factors, one should summarise that there are many factors moulding developmentalist patterns of countries, which cannot be deduced only from economics realm, since non-economic factors have also determining roles to a large extent. In our study, hence, we take into consideration the political economy, legal and societal factors along with commonly referred economic factors. Accordingly, an empirical study is conducted, in the next section, by considering the relevant literature to determine the most appropriate indicators of Islamic banking development and economic development nexus, which, in return, is expected to provide an original study. Prior to this, a brief literature on Human Development Index or HDI-related studies should be reviewed here (Table A.2.7 is created in the appendix listing HDI-related studies in detail) for it gives us the opportunity to compare and contrast the main motivation for including HDI as dependent or independent variable in empirical growth studies. By doing so, it is possible to authenticate this study's contribution to the literature through placing HDI into the agenda of Islamic banks' developmentalist goals.

2.3.2.3. Human development as an exclusive factor

As mentioned before, this study aims at deploying HDI as a benchmark for economic development in an attempt to examine the performances of selected Islamic banks with regards to their contribution to developmentalist trajectories of countries. In the entire literature, however, HDI is scarcely chosen either for the variable explaining economic growth, or dependent variable that is explained by some combination of different factors. It is this study's novel attempt that neither of the studies attempted to consider HDI to include as the dependent variable in Islamic banking performance studies.

Once looking at the relevant literature, HDI is mostly associated with financial development in order to empirically examine the impact of the growth of financial sector in certain economies on HDI (*see*: Asongu and Nwachukwu 2015; Monacelli, Iovino, and Pascucci 2012; Ostojic, 2013). In these studies, it is unanimously found that financial development has strong positive relationship with human development, implying a substantial role attached to financial sector in fostering economic development.

There are also two particular studies considering HDI as one of the control variables for the dependent variable of financial development (*see*: Filippidis and Katrakilidis 2015; Outreville 1999). The results, in each study, suggest that HDI contributes to financial development significantly.

A time series study is conducted by Sehrawat and Giri (2014) to determine the direction of causality between financial development and human development in India between the period 1980-2012. It is concluded that there is a unidirectional relationship between these variables running from financial development indicators to human development index.

As evident from the discussed empirical contributions, human development aspects are hardly incorporated in the finance-development literature hitherto. Acknowledging this gap in the related literature, this study introduces a novel approach to finance-development studies by examining Islamic banking and human development nexus. By doing so, the so-called superior notion of GDP as the ultimate benchmark for economic growth is replaced by HDI, which is believed to reflect relatively more appropriate measure of social welfare despite the debated nature and contested contents of HDI.

2.4. ISLAMIC FINANCE AND ECONOMIC DEVELOPMENT IN FINANCE-GROWTH AXIS: A CRITICAL PERSPECTIVE

As discussed in the preceding section, the nature, direction and implications of finance-growth nexus have been debated thoroughly for the last couple of decades in the conventional literature. Except some critical approaches by heterodox schools of economic thought, advancement in financial sphere is generally posited to accompany economic growth and development. With the significant ascent of neoclassical thought and its permeation through the global economy in 1980s, the potential of finance over economic performance has further been essentialised in that finance has gained an autonomous sphere within the economy (which is discussed in great detail in the next chapter, Chapter 3, under financialisation debate), and the overall economic development hinged on improvements in the financial sphere. Once the idea of finance-intensive policies of economic development was adopted, it accompanied the identification of parameters of global financial development with the measures of financial depth, access, efficiency and stability (Čihák *et al.* 2012). As a consequence of such dialectic as part of neo-liberal policies, every country has been conditioned to follow and apply the agenda of global financial development so long as it aims to enhance its economic condition.

Recalling the political economy debate on the role of Bretton Woods institutions, the post-modern phase of universal development ideology stipulated a finance-centred economic development understanding. The essentialisation of finance, therefore, is not a coincidental emphasis imposed on developing world, but rather a new form of preserving world income and resources in the hands of financial incumbents through transnational institutions. Global economy, in this sense, has been reorganised around the pursuit of financial profits in the wake of profitability crisis suffered within real economic activities (Lapavitsas 2013:2; Tauss 2012:55). Thus, financial sphere has been expanded to exacerbate redistributive injustice. This is evident in the statistical records of world income distribution and profits generated through financial transactions. In addition, the gap between the size of real and financial assets in the global economy (Epstein 2005; Greenwood and Jovanovic 1990) affirms the convergence towards finance-led growth theories.

Banking system, amid the ascendance of finance, plays a crucial role in financialised economy, since an economic system dominated by the ambition of generating financial profits necessarily shapes banking sector and its operational structure. Therefore, conventional banks, from its outset, were organized in pursuit of shareholder value maximisation through concerning and engaging in most profitable and efficient economic activities. Their contributions towards social aspects of economic life are taken as granted and hence have scarcely been examined within mainstream debate. Even worse, the neo-classical paradigm does not consider social impact as evident in Friedman's famous magazine article titled as "the social responsibility of business is to increase its profits" (Friedman 1970). In this view, financial development is believed to generate good society as long as economic activities become subservient to financial profits and efficiency dominates economic and financial activity.

Islamic finance emerged and flourished, not by chance, in the 1970s wherein finance-led growth theories beset and influenced alternative views and perspectives of economic understanding beyond mainstream economics. Contrary to the conventional system and its autotelic objectives ignoring the notion of 'social impact finance', as explained above, Islamic banks manifested to play an important role over contents, goals, substance and achievements of the development process in Muslim-dominated countries. Thus, as the detailed discussion above identified, Islamic banks have been charged with the realisation of the theoretical conceptualisation of IME in delivering Islamic development objective, with an imagined role to have high impact on both individual well-being and social welfare.

In considering the performance throughout the forty years since its inception in 1975, beside the aspirational dimensions of IME, initial objectives attached to Islamic banking have been challenged entirely by market oriented professionals and some scholars of Islamic finance on the grounds that to what extent it is possible to differentiate the financial logic of Islamic banks from its counterparts and hence can gain authenticity by reforming its organisational structure as a social banking system. As the term 'bank' cannot be translated into any language other than pronounced as 'bank' in every language, similarly, the organisational structure, aims and functions of banks are kept substantially similar in different societies. Thus, the objectives of banks around the world, regardless of being Islamic or conventional, should necessarily respond to the maximisation of profit and adaptation upon the competition rules of market system. This argument explicitly asserts that, an Islamic bank would, at best, generate social impact in an eclectic and auxiliary manner as by-product rather than the impact emerged as a natural outcome of embedded part of economic system.

Throughout forty years after its inception, Islamic banking and finance is now critically examined due to its divergence from developmentalist promises and converging towards non-developmental expansion of its activities in parallel with the prevailing global financial system (Abdul-Baki and Uthman 2017; Asutay 2007b, 2012; Cebeci 2012; Mansour, Ben Jedidia, and Majdoub 2015; Platonova 2013). Finance, like any other system in economy, is expected to generate social good in order to achieve good society (Shiller 2012); otherwise, it would cause disaster not only in economic sphere, but also in social, political and cultural areas such as the case with the global financial crisis in 2007. Islamic finance is, now, similarly, critically approached to bring back the value-driven motivation behind its emergence (*see*: Al-Jarhi 2005; Iqbal and Mirakhor 2013a, 2017). If it had operated in line with its normative characteristics, Islamic finance would have now been considered as a strong financing system that can respond to the globally raised issues in the wake of the recent social failure of mainstream financial system.

Recalling of Islamic developmentalism, after recognising the social failure of IBF, ensured that Islamic finance should abandon trusting only on contractual level analysis, and bring forth the social implications in harmony with *fiqh* and morality. Its main contribution to development as a development-oriented institution, hence, should be on serving as community banking for individuals and societies, rather than markets (Asutay 2007b). By the emphasis on such characteristics of Islamic finance, the preceding section surveys conventional literature on the relationship between finance and economic growth to provide a comparative analysis by exploring how mainstream finance is envisaged to impact economic growth, whilst, on the other hand, Islamic finance would make significant difference by contributing to the fulfilment of developmentalist objectives.

The justification of Islamic banks' social failure in terms of not contributing to social good in an embedded manner through such an argument stems from the espousal of a universal understanding of finance and banking system, which, in fact, captivates and hampers the emergence of alternative views on how finance should be dealt in everyday practice to generate developmentalism beyond its prevailing function. It should, thus, be recognised that the modern financial system is a socially constructed reality that has been shaped throughout the modern period to constitute a new form of capital accumulation in the age of 'finance capitalism'. In acknowledging this, an alternative approach upon financial sphere is argued for irrespective of existing mainstream financial structure. Therefore, this discussion in this section urges, first, to consider the activities of Islamic banks not as simple financial intermediation, but rather business models, as historical applications of Islamic financing modes were business ventures and not financial modes. The replacement of intermediation with business stakeholding gives some responsibilities to Islamic banks, as active agents, in evaluating the consequences of contracts in terms of their contribution to value-added in real economy. In a simple *murabahah* contract, for instance, bank should reckon with its role in value adding through the potential benefits of contract upon economy and society, rather than confining itself with providing financial intermediation. Once performances of Islamic banks are re-examined from this angle, their success or failure in generating social impact would no longer remain beneath the surface; thereby, it paves the way for examining Islamic financial contribution.

The construction of financing activity in Islamic paradigm, secondly, necessitates approaching finance as an everyday practice rather than a self-proclaimed and sophisticated mechanism resulting in commercialised and financialised economy. In doing so, simple function of financing becomes subservient to the whole idea of development with the pursuit of creating 'good society' (Shiller 2012). Financial activities, in this manner, should not only be subject to financial performance; instead, their social performance should also be examined to what extent Islamic financing activities are conducive to generate good society.

While the applications in the sector evidence that Islamic finance is a hybrid financial proposition basically operates with the same motivational frame of its conventional counterparts (Asutay 2012), the objectives of Islamic banks in spurring economic development were identified in such a developmentalist manner in the initial literature. Thus, the early contributions in the 1980s invariably extolls the experience of Mit Ghamr as a social bank based on profit and loss sharing (*see* the related studies: Asutay, Aysan, and Karahan 2013; Chachi 2005; El-Gamal 2007; Hegazy 2006; Kahf 2004; Mayer 1985), and hence, emphasises its role in generating an economic uplift in the conditions of the poor through expanding capabilities and capacities as envisaged by IME. Thus, the authentic institutional logic of Islamic principles relating to economy and finance refers to an organic emergence of Islamic institutions which can be a reflection of the Islamic order and worldview. The latter refers to a particular economic paradigm and modes of production within *tawhidi* world defined by the actualisation of Islamic economic axioms. Such actualisation by definition implies that any institution shaped by such features has to be stakeholder oriented with the aim of developing participatory economy through risk-sharing and profit-and-loss sharing. Consequently, an Islamic bank is expected to work within such an institutional logic in essentialising the Islamic modes of production in order to be authentic and emergent (*see*: Asutay 2018).

Amongst the developmentalist features of Islamic finance, direct attention is given to its asset-backed and equity-based nature as part of linking to productive or real economy, profit and loss sharing, promoting risk sharing through trading and diversifying risks, mobilising and pooling of savings for investment, improving access to financial services, resilient finance through ensuring stability of banking sector and financial markets, avoidance of non-permissible transactions such as alcohol and pornography (*see*: Asutay 2010, 2015; Hassan and Lewis 2007; Iqbal and Mirakhor 2013; Kettell 2010; Syed Ali, Shirazi, and Nabi 2013; Warde 2010, amongst others). These can be considered as characteristics of Islamic finance that have implications within the financial sector.

As mostly been emphasised, based on such features, Islamic banks are ideally expected to be driven by the motivation of profit and loss sharing and risk sharing so that a participatory nature of finance would come into existence as contrast to interest-based financial system that poses inequalities in the societal level. Similarly, Islamic financing transactions have to be backed by an asset to relate it with real economy. In other words, every Islamic mode of financing has to add value upon the economy through capital transfer and its circulation in *Shari'ah* compliant ways. It is also expected that the savings are pooled in Islamic banks to be allocated and channelled into socially beneficial investments, which, in return, would encourage Islamic entrepreneurship. Islamic banks aim to reach everyone irrespective of income level so that financial access and inclusion should lead to development in both individual and societal level.

Despite these aspirations were associated with Islamic banking and finance, the applications reveal a great divergence between ideals and realities that culminates in hybridity and mimicry. As Islamic finance is relegated to and considered within contractual level, its social implications are neglected without consequentialist manner by emphasising form over substance. *Maslahah* (public interest) instead, has taken the role of integrating Islamic finance into global financial system through *fiqhi* process as evidenced in *tawarruq* contracts, as delusional *maslahah* has instrumentalised the Islamic morality in justifying the mimicry. As the thorough examination regarding the divergence from social aspirations of Islamic finance is addressed in the next chapter (Chapter 3) under Islamic financialisation, this chapter in the next section examines whether the observed developmentalist failures is evidenced through empirical study.

2.5. ISLAMIC BANKING AND ECONOMIC DEVELOPMENT NEXUS: ECONOMETRIC ANALYSIS

Based on the discursive analysis presented in the preceding sections, this section aims to develop and test an empirical model to examine as to whether Islamic banking contributes to multi-faceted economic development as aspired by IME.

This section attempts to assess the relationship between Islamic banking growth and economic development through an empirical analysis by constructing a panel data analysis of 21 countries with observed Islamic banking presences over the period of 2003-2014. Since developmental outcomes can only be observed over a long-run period, we opted for using yearly data instead of averaged data such as 3-year or 4-year intervals, as interval-based data smooth distribution of time dimension and hence may miss out short-term influences of development trajectories.

The structure of this empirical part is inspired by Imam and Kpodar (2016) in which potential contributions of Islamic banking growth on economic growth is examined empirically by including several aspects of the relationship with different econometric applications. In parallel with this structure, in the empirical model in this chapter, first, the baseline regression aims to examine the relationship between Islamic banking growth and economic development wherein three alternative indicators of Islamic banking growth regressed separately and a standard proxy for overall banking development is used as one of the explanatory variables.

In the second stage, a number of alternative empirical analyses were conducted to test robustness of the relationship. In specific, alternative variables are selected for overall banking/financial system development, and the impact of Islamic banking growth is re-examined. Additionally, we changed the sample size based on the share of Muslims in population of country and proceed with another regression. Lastly, sample size is reorganised once again to include only oil rich countries with the aim of observing the impact of oil factor over Islamic banks' growth and performance.

It should be noted that data availability constrained the general sample size and the selection of variables, as Islamic banking data is quite limited and scattered in various databases with its basic indicators.

The following section describes the variables of the model in relation to the Islamic banking growth and economic development, the information set and basic summary statistics and correlations. Then, the next section provides a thorough explanation of the research methodology where several econometric techniques are explained, and regression results are interpreted.

2.5.1. Variable Definition and Model

Beyond a standard growth model with a set of mostly used measuring of banking/financial development and growth,[10] this study aims to locate development-oriented indicators for dependent, independent and control variables. Further to the data sources shown in Table 2.1, the variables and their identification are listed and explained below:

[10] To give an example of generally used indicators of financial development and economic growth in the mainstream literature, we constructed Table A.2.9 in the appendix.

(i) Economic Development: Human Development Index (HDI)[11] is chosen to measure economic development, since it seems to be the most appropriate indicator amongst very limited alternatives which goes beyond growth perspective. Not just appropriateness but also the data availability of selected countries was a concern to choose HDI, as we would otherwise tend to consider other development-oriented variables such as Inclusive Wealth Index, OECD Better Life index, Sustainable Development Index, World Development Index, World Happiness Index, Inequality-adjusted HDI, Multidimensional Poverty Index, GINI index and so on.

Despite the fact that HDI is hardly chosen in the finance-development literature and this makes our study an original attempt, the rationale behind the selection of HDI coming out of the lack of better alternative indicator for economic development, accompanies with some serious limitations in reflecting economic development. For instance, it is widely emphasized that HDI omits some important dimensions of development on both individual and societal level, environmental and safety issues with some further micro dimensions such as housing quality, pollution, crime rates, unemployment, quality and of goods and services, quality of education.[12] In addition, it can be argued that financial institutions cannot have a direct impact on HDI, since its components of education and health are hardly affected by financial sector. Therefore, the attempt to attach Islamic banks a role to contribute to HDI may sound irrelevant. However, as the endogenous growth theories implicitly evidence, financial institutions can have great impact on social aspects of economic life, since financing health and education is no longer depended upon the public sector entirely in developing countries, but rather became investment areas to seek profit especially after the privatization process. Furthermore, Islamic banks within the aspirational paradigm are expected to contribute to human-centred development and therefore their presence in social areas such as health and education is by definition is expected. Thus, when choosing HDI as dependent variable as a proxy for economic development, we acknowledge all these problems and register our reservations on HDI. This fact is also considered for the interpretations of the variables and their impact on human development.

[11] HDI, as a composite index, aggregates country level attainments in life expectancy and education, as well as income. From 2010 onwards, two of the three dimensions of HDI has altered. Accordingly, life expectancy remained unchanged, while gross national income (GNI) has replaced GDP and literacy and the gross enrolment rate -as used in the old HDI- have been replaced by mean years of schooling and the expected years of schooling. From 1990 to 2009, the HDI gave equal weights to three functions of its core dimensions for health, education and income. However, from 2010, instead of using arithmetic mean HDI values is calculated by using geometric mean. The rationale for this change is due to allowing for imperfect substitutability between the HDI's three components.

[12] For a brief history of HDI critiques, see UNDP review paper by Kovacevic (2010).

(ii) Islamic banking growth: Since financialised view of economy is widely taken for granted in empirical research areas, most of the researchers consider the extension of loans/financing by Islamic banks as the indicator for Islamic banking growth (Bashir 2003; Gheeraert and Weill 2015; Goaied and Sassi 2010; Grassa and Gazdar 2014). However, in line with theoretical suggestions, the amount of credits/loans/financing given does not guarantee the productivity of economy, for these loans might be spent unproductively. More sophisticatedly, unregulated loans and credits extended to individuals can culminate in high indebtedness of households and corporations, which, in return, can create a debt society through the destruction of social balance and harmony at the expense of capitalist interests.

In the light of this aspect of credit extension, we consider 'total financing values of Islamic banks divided by nominal GDP' as the indicator for Islamic banking growth. In addition, alternative indicators are considered as 'total assets of Islamic banks to nominal GDP', 'total deposits of Islamic banks to nominal GDP', and lastly 'total investment of Islamic banks to nominal GDP[13]'.

More sound variables could be constructed if there was no data availability and disclosure problems within Islamic banking sector. In acknowledge of this, selected indicators examine to what extent ethics-based mode of Islamic financing contributes to economic development through facilitating risk sharing, enhancing financial stability and strengthening real sector. We assume that performance of Islamic banks should render no significance over development process as they invariably mimic conventional banking understanding that aims financial performance with negligence of social performance.

(iii) Development of the overall banking sector/financial system: Similar to the variables of Islamic banking system, overall banking and financial system development is measured by credits, assets and deposits of conventional banks as a share of nominal GDP. In this regard, 'credit by deposit money banks to the private sector divided by GDP' is used as an indicator of overall banking development for the baseline regression. Furthermore, the alternative variables are 'assets of banks and other financial institutions to GDP', 'private credit by banks and other financial institutions divided by GDP', and 'financial system deposits to GDP' are used in different regressions as benchmark for financial system development.

[13] As mentioned before, Islamic banking data availability is an important task that needs to be overcome. In relation to this, we could only find these variables in a website called 'IBIS online' which operates under Islamic Research and Training Institute. However, the problem is that the data does not cover the periods after 2013. Thus, we confine ourselves with the available data.

Table 2.1: Definitions and Sources of Variables

Variable	Definition	Source
HDI	Human Development Index	United Nations Development Programme (UNDP)
Islamic Banking Growth	(i) Financing by Islamic banks to GDP (ii) Assets of Islamic banks to GDP (iii) Deposits of Islamic banks to GDP (iv) Investment of Islamic banks to GDP	Islamic Banks and Financial Institutions Database (IBIS Online)
Overall Banking Growth	Credit by deposit money banks to the private sector divided by GDP	Beck, Demirgüç-Kunt and Levine (2000); 2013 Financial Development and Structure Dataset
Overall Financial Development	(i) Private credit by banks and other financial institutions divided by GDP (ii) Financial system deposits to GDP (iii) Financial system assets to GDP	
GDP per capita	Change in the ratio of real Gross Domestic Product (GDP) divided by the size of the population.	World Bank (Word Development Indicators)
Trade openness	The sum of exports and imports of goods and services measured as a share of GDP.	
Oil rent	Oil rents are the difference between the value of crude oil production at world prices and total costs of production as a share of GDP.	
Rule of Law	The confidence of citizens in law, and the extent that they abide by the rules of the society, such as contract enforcement, property rights, police, and court.	World Bank (World Bank Governance Indicators)
Political Stability	Perceptions of the likelihood of political instability and/or politically-motivated violence, including terrorism.	
Industrialisation	Manufacturing value added as a share of GDP	United Nations Industrial Development Organisation (UNIDO)

As most of the heterodox schools critically approach, the effect of conventional banking system over economic development patterns of countries is somewhat contested issue in the sense that the growth of total asset, credit and deposit values of conventional banks can be considered as the implications of non-developmental expansions of banking system, which can be interpreted as insignificant impact on HDI values of countries. It is further criticised that conventional banking would also have negative consequences on HDI due to the detrimental effects of financialisation process in which real economy does not fulfil its role in contributing to income smoothing or alleviating poverty amongst the poor.

After identifying the main variables, the control variables are defined as follows:
(i) GDP per capita growth is used to reflect the extent of material output or total income that a particular country distributes to its citizens; and generally accepted as perfect indicator for evidencing the advancement of countries. Therefore, an increase in the GDP per capita growth would make high positive impact on HDI through boosting the material wealth of individuals. However, in fact, the calculation of GDP per capita values predicates on mathematical measurement; thereby an increase in GDP, including its per capita and growth dimensions, does not guarantee improvement in wealth distribution in the population in practice.[14] This implies that the increase in GDP per capita would give negative implications for human development in countries where GDP growth widens the gap between the poor and the rich through its accumulation in the hands of few riches.

On the practical side, it is obvious that some countries are falling behind in the HDI ranking at a certain period of time while they perform significant increase in GDP levels in the same period. For example, Qatar has top ranking in GDP per capita (PPP) terms in 2016, while it has 33rd position in the HDI ranking (United Nations Development Programme 2016).

In recognition of this, we normally expect a positive impact of GDP per capita growth on economic development; however, considering the distributional issues being problematic in the selected sample lead us to assume adverse effect of the variable on HDI. One way to shed light on distributional relationships in countries is to employ GINI variable as an indicator for the degree of income inequality. However, the relevant data is quite limited with advanced countries, thereby we are unable to locate GINI data for our sampled countries.

(ii) Trade openness: Defined as the sum of imports and exports of goods and services measured as a share of GDP, advantages of an open economy are heatedly debated in the literature. According to the proponents of financial liberalisation (*see*, for instance, Goldsmith 1969; Gurley and Shaw 1955; Hicks 1969; McKinnon 1973; Shaw 1973), trade openness would make

[14] For a thorough explanation of GDP, its political economy and historical significance, *see*: Coyle (2014).

great impact on growth and development, since it leads to benefit from economies of scale in production in an efficient manner. Nevertheless, mainly Marxist theorists and dependency approach assert that this argument is valid only for advanced countries, for they can easily integrate in the global economy and enjoy economies of scale through their multinational corporations' (MNCs) activities of import and export. Less developed countries, on the other hand, are highly vulnerable to external shocks and crisis since their economic stability is fragile and high economic performance hinges on global economic trends. In favour of this approach, trade openness is assumed to reveal negative consequences for economic development.

(iii) Oil Rent: Oil production and its rent play a significant role in our sample countries such that a large portion of income accumulates in the sample countries from oil money or petrodollars. Thus, it is normally expected that oil rent expands the capacity of domestic economy through providing capital for domestic investment opportunities, and an increase in total wealth with the effect of oil money should enhance individual wellbeing and social prosperity. However, positive correlation between oil richness and income inequality evidences that oil production makes gains exclusively for upper class or royal families in the case of Middle Eastern and GCC countries. The regression results, under this assumption, aims to demonstrate the extent to which oil rent contributes to HDI through increasing overall economic performance and total income.

(iv) Industrialisation: When the dynamics of economic development are considered in modern economies special importance is given to industrial performance due to a strong relationship between industrialisation and economic wealth. Developing world, in this manner, follow the footsteps of advanced countries to replicate the development process through industrialisation. Whilst we keep our reservations about potential adverse impacts of industrialisation on socioeconomic life and moral character of economy, it is still valid argument that industrialisation and its share in GDP is an essential concern for material development since it deals with real economy and produces value as compared to financialised economy wherein finance remains standalone sector in the overall economy and has nothing to do with real economy. Due to such a reason and considering the weight given by HDI components to material aspects of wealth, we expect a positive effect of industrialisation on economic development.

(v) Rule of Law: Based on the statement that development is a multifaceted concept, there should be non-economic parameters influencing development trajectory of countries. Amongst many others, rule of law reflects one of the political economy aspects of development and

captures perceptions on rules and social contracts and its enforcement and regulation of social life. It might be perplexing that rule of law has close affinities with legal systems. However, in fact, rule of law takes into account the consequences of the application of laws that prevailing in the national law system irrespective of the adopted legal system such as British and Dutch legal system. In other words, as a variable, rule of law, captures the perceptions and confidence of citizens on rules and social contracts and its enforcement and regulation of social life irrespective of the adopted legal system. In this manner, it is expected to have positive and significant relationship with HDI.

(v) Political Stability: This variable helps crystalize the impact of political stability/instability on the developmentalist objectives of countries. The nature of political regimes is worthy to note, for political instability or unrest can have a positive developmentalist impact in non-democratic regimes through enabling justice in redistributive channels, which may tend to close the gap between the poor and the rich (for the studies searching for the impact of political regimes on economic growth, *see*: Table A.2.6 in the appendix). Thus, political reform can redesign wealth distribution in a best way by weakening the power of financial or political incumbents and uplift the socioeconomic conditions of middle and lower class.

Based on the variables defined, the baseline regression is formulated as follows:

$$H_{it} = \alpha + \beta ISBD_{it} + \gamma FD_{it} + \delta X_{it} + u_i + \varepsilon_{it} + v_t \qquad [2.1]$$

where *H* is the Human development index values; *ISBD* is the indicator for Islamic banking development; *FD* is the measure of overall financial development; *X* is the set of control variables described above; u is the country-specific effect, ε the error term and v is the time-specific effect.

Table 2.2: Country Sample & Share of Islamic Banks in National Economy*

Bahrain	13%	Kuwait	39%	South Africa	1% - 2%
Bangladesh	19.5%	Lebanon	0% - 1%	Sudan	100%
Bosnia	0% - 1%	Malaysia	23.8%	Tunisia	5.5%
Egypt	8%	Pakistan	12%	Turkey	5.5%
Indonesia	5%	Palestine	11%	United Arab Emirates	19.6%
Iran	100%	Qatar	26.6%	United Kingdom	0% - 1%
Jordan	15.2%	Saudi Arabia	51.1%	Yemen	30%

Note: * The shares are transformed into numerical values from the graph provided in IFSB Stability Report (2017:8).

2.5.2. Empirical Process and Method

In the light of the aim of developing a distinct analysis to developmentalist consequences of Islamic banking expansion, this study employs a quantitative methodology to examine the developmentalist contribution roles of Islamic banking, if any, on development trajectories of countries through measuring and comparing performances of Islamic banks. Thus, an attempt is made to explore the relationship between Islamic banking growth and economic development through an unbalanced panel data analysis[15]. It is true that a vast number of empirical studies examine the relationship between Islamic banking growth and economic growth; however, this study aims to take the debate one stage further by bringing developmentalist consequences of Islamic banking into question in line with the IME expectations.

Since this research is based on econometric study, it makes use of historical statistical data. Through interpretation of the data, possible explanations for the impact of growth of Islamic banking sector on the quantitative aspects of developmentalist oriented aims is sought by sampling Islamic banks from 21 countries. In carrying out the analysis, a development-oriented index (HDI) highlighting the quantitative parameters is considered and this enables us to test performances of each Islamic bank with regard to their promotion of individual wellbeing and social welfare. For the outcome, resulting trends of Islamic banks can verify or falsify if they comply with the aforementioned developmentalist objectives.

Before presenting regression, the results and interpreting them, it should be highlighted that conducting a panel study on Islamic finance growth-development nexus incorporates several econometric challenges. Firstly, Islamic financial operations can be traced back to very recent times and the data availability is a well-known issue to be addressed; hence, a long-run project development can hardly be evaluated by analysing short-run time period with the limited data. Secondly, despite its distinctiveness, HDI does not constitute an ideal indicator for our study as it poses many problems (*see*, the related studies: Chowdhury 1991; Noorbakhsh 1998; Posner 2007; Ravallion 2012). However, it still seems to be the best indicator for empirical development studies. Thirdly, Islamic banking sector has limited share within the respective national financial system in some of the sampled countries. In addition, the size of Islamic banking sector is small in comparison to the conventional banking system in all cross-country

[15] The rationale behind choosing panel data analysis comes from the fact that Islamic banking operations are present across many countries; thereby, instead of applying time series analysis with just one cross section of country, panel data allows us to include observations from different countries. By doing so, it is possible to examine wider applications of Islamic banking in different regions.

samples. Therefore, it might seem, at first glance, that we should not expect a significant impact from Islamic banks on the overall economy. However, IFSB (2017:8) clearly asserts that "those [countries] that satisfy the criterion of having a more than 15% share of Islamic banking assets as a proportion of their total domestic banking sector assets … are categorised as systemically important". Based on this argument, half of our sample countries seem to have Islamic banking sector that is systemically important in their financial system, as illustrated in Table 2.2. Although the rest of the countries are unable to reach systemic importance, considerable growth of the sector in these countries should give some implications about its contributions to the development trajectories of the respective countries.

It might be tempting econometrically to apply two different system-GMM regressions by splitting data into two categories, one of which takes only those countries that have Islamic banking shares over 15% within the national economy; and those countries that could not reach systemic importance, hence remain below the 15%. Based on the rule of system-GMM, which states that the cross-section dimension (N) has to be larger than the time dimension (T), we have only 10 countries that have Islamic banking shares over 15% within the national economy. Thus, maximum 9 years can be considered for the empirical analysis, which, in return, makes our dataset consisting of 90 observation. Since 90 observation is not sufficient in applying system-GMM as the rule suggest to get reliable results, the idea of conducting two different regressions by including only countries with systemic importance is given up.

A range of econometric techniques is utilised, by acknowledging these challenges, including pooled and fixed effects estimator that enables us to control country specific effects, and the system-GMM estimator to address endogeneity bias through controlling it. Together with interpreting the results, the next section provides rationale for choosing these estimators to compare, and also the econometric advantages and disadvantages of each estimation technique.

2.5.3. The Results of Econometric Estimation

Table 2.3 and Table 2.4 respectively present summary statistics and correlation matrix for the variables used in the econometric analysis in this study for 21 countries observed during the period 2003-2014.

As can be seen in Table 2.3, a relatively wide gap between the minimum and maximum values of variables[16] is in evidence for Islamic banking growth, overall banking and financial development,[17] trade and political economy variables, namely rule of law and political stability. This shows that Islamic banking performances vary significantly amongst the sample countries together with their political economy structures and trade openness. While the share of industrialisation does not differ much across the dataset over the years, oil rent as a share of GDP seems to constitute a considerable amount of national income. In addition, it can be deduced from the table that conventional financial system holds a considerable claim in the GDP of most of the sampled countries, which means that banking and financial institutions plays a central role in economy.

Table 2.3: Summary Statistics

Variables	Obs.	Mean	S.D.	Min	Max
Human development index	252	0.699	0.119	0.415	0.908
Financing by Islamic banks/GDP	252	0.081	0.106	0.000	0.484
Assets of Islamic banks/GDP	252	0.155	0.236	0.000	1.450
Deposits of Islamic banks/GDP	252	0.100	0.129	0.000	0.854
Investments of Islamic banks/GDP	252	0.114	0.171	0.000	0.905
Assets of banks and other financial institutions/GDP	252	80.269	49.659	8.705	212.276
Credit by deposit money banks to the private sector/GDP	252	50.836	35.485	4.106	202.200
Private credit by banks and other financial institutions/GDP	252	56.674	40.424	4.106	202.200
Financial system deposits/GDP	252	64.234	48.962	7.417	245.428
GDP per capita growth	252	2.009	4.201	-15.038	15.952
Trade openness	252	82.389	41.209	19.459	210.374
Industrialisation	252	0.128	0.048	0.047	0.265
Oil rent	252	10.639	15.139	0.000	60.236
Rule of law	252	47.162	22.428	2.871	95.694
Political stability	252	31.042	24.727	0.474	92.462

The simple illustration of correlation matrix in Table 2.4 shows that HDI has high positive correlation with rule of law, political stability and credit by deposit money banks to the private sector to GDP ratio, all of which are close to but not exceed the level of 0.70, which is considered as rule of thumb for efficient estimations in empirical studies. Correlation of variables for Islamic banking growth with HDI, on the `other hand, remains between 0.20 and

[16] It might be argued as to whether the empirical results give biased implications due to the potential outliers used in the dataset. Based on such a consideration, the data is winsorised by removing the potential outliers, and the regression is repeated. However, it is empirically evidenced that the results did not change after winsorisation.
[17] The relatively large maximum numbers for Islamic and overall banking development in the table is due to the significant share of Islamic banking assets in the GDP for particular years in the case of Bahrain, and financial development indicators in the United Kingdom that go beyond GDP values.

Table 2.4: Correlation Matrix

		(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)
(1)	Human development index	1.000														
(2)	Financing by Islamic banks/GDP	0.286	1.000													
(3)	Assets of Islamic banks/GDP	0.278	0.894	1.000												
(4)	Deposits of Islamic banks/GDP	0.200	0.957	0.855	1.000											
(5)	Investments of Islamic banks/GDP	0.275	0.931	0.967	0.915	1.000										
(6)	Assets of banks and other financial institutions/GDP	0.450	-0.035	-0.003	-0.075	-0.008	1.000									
(7)	Credit by deposit money banks to the private sector/GDP	0.626	0.057	0.047	0.017	0.044	0.774	1.000								
(8)	Private credit by banks and other financial institutions/GDP	0.550	0.060	0.090	0.016	0.087	0.863	0.920	1.000							
(9)	Financial system deposits/GDP	0.452	-0.070	-0.063	-0.094	-0.070	0.781	0.728	0.610	1.000						
(10)	GDP per capita growth	-0.224	-0.182	-0.165	-0.139	-0.157	-0.170	-0.175	-0.170	-0.114	1.000					
(11)	Trade openness	0.531	0.375	0.379	0.334	0.387	0.239	0.352	0.313	0.282	-0.158	1.000				
(12)	Industrialisation	-0.023	-0.043	-0.007	-0.038	-0.023	0.072	0.126	0.119	0.017	0.183	0.226	1.000			
(13)	Oil rent	0.167	0.356	0.224	0.369	0.272	-0.285	-0.201	-0.196	-0.307	-0.144	0.095	-0.446	1.000		
(14)	Rule of law	0.620	0.239	0.230	0.178	0.231	0.007	0.307	0.158	0.124	-0.148	0.562	-0.067	0.210	1.000	
(15)	Political stability	0.692	0.167	0.105	0.098	0.118	0.275	0.457	0.451	0.138	-0.206	0.497	-0.046	0.261	0.651	1.000

0.30 as compared to that of overall banking and financial development variables standing between 0.45 and 0.60. It is quite interesting that GDP per capita growth has negative correlation with the rest of variables in the model without exception. Overall, there seems no problematic relationship amongst variables which would threaten the reliability of the model and weaken the trust on the regression results.

2.5.3.1. Pooling and fixed-effects estimators

Table 2.5 presents the results of pooled-OLS and fixed-effects regressions models, which covers the period 2003-2014 for 21 cross section of countries and the dependent variable is HDI. While the pooled-OLS estimator disregards country specific data by pooling available data in one basket and runs it accordingly, fixed-effects estimator, on the other hand, controls for unobservable country specific and time independent effects. In other words, it is a particular method to eliminate time invariant unobserved effects in a regression model.

As can be seen in Table 2.5, the models 1 to 6 show the results of pooling estimation, while the rest of models (6 to 12) show that of fixed-effects estimation. The baseline regression model in each estimation (model 1 and 5) is run only with the control variables, which are determined as GDP per capita growth, trade openness oil rent, industrialisation, rule of law and political stability. Then, overall financial development variable is controlled in model 2 and 8 and the regression is re-run to observe how the results alter after adding the new variable. Lastly, 3 variables of Islamic banking growth are sequentially introduced in models (3 to 6) and (9 to12) to control the effect of these variables over the model.

Initial findings in the pooled-OLS regression suggest that Islamic banking growth variables are all positively significant – except for Islamic bank deposit to GDP - over HDI, and the coefficients are quite high as compared to other variables. Overall banking development is, on the other hand, invariably significant in all models, yet its impact on HDI remains limited with 0.14% while that of Islamic banking growth has 11.5%, 6.8% and 8.5%. Thus, the models imply that both Islamic and conventional banking growth stimulate economic development with the former having superior impact. Looking at the macro variables, it is seen that rule of law, political stability, oil rent and trade openness show positive significance nearly in all models with small impact on HDI ranging between 0.03% to 0.22%. Amongst them, trade openness is in parallel with the findings of finance-growth literature and suggests further financial liberalisation to increase development. Nevertheless, the effect of GDP per capita growth and industrialisation is negative and insignificant, weakly implying a counter result to the expected relationship of these variables with HDI. The first model helps explain 55.6% to 68.3% of the variability in economic development rates.

It should be noted, here, that the overall results of pooled-OLS estimator rendered in our dynamic panel data model may not be reliable, since OLS approach does not account for simultaneity bias or unable to control for country fixed effects in such regressions. For this reason, we also conducted fixed-effects regression model and the most superior technique of system-GMM to get more robust and reliable results. The rationale behind choosing fixed effect model instead of random effect in our regression analysis comes from the results of Hausman test, which is applied to ascertain about the right estimation method for the data. Table A.2.10 in the appendix shows the results of Hausman test. The p-value of 0.000 means that the null hypothesis is rejected, and hence fixed effect model is, as a result, considered appropriate for our model.

The right-hand side of Table 2.5 shows six different models estimated with fixed-effects method. It is hard to claim that the results of each variable hold similar coefficients and significance levels with that in the pooled-OLS estimation results. Contrarily, conventional and Islamic banking growth turns out to be insignificant over economic development trajectories. In the same vein, rule of law and political stability becomes no longer significant, and the latter weakly implies an adverse effect on HDI. However, the relationship between industrialisation and HDI turn out to show parallel with our initial expectations in that the sign of the coefficient changes to positive. Other variables remain mostly the same, only oil rent keeps its significance but with a negative impact, which can be understood as oil richness does not guarantee economic progress and human development as the HDI levels of the GCC countries prove. Overall, the models help explain 10.9% to 15.4% of the variability in human development ratios.

2.5.3.2. System-GMM estimator

In addressing the endogeneity issue, this study trusts the panel system-GMM estimator[18] developed by Blundell and Bond (1998), which uses both the difference panel data and the data from the original levels specification that eventually enables us to produce dramatic increases in both consistency and efficiency. As an alternative to system-GMM estimator, difference-GMM could be adopted; however, it raises the serious problem within its estimation that

[18] A useful guide for the application of the system-GMM estimator on growth models can be found in Bond, Hoeffler, & Temple (2001).

includes (i) the elimination of the cross-country relationship and focusing only on time differences, (ii) the suffer from imprecision and potentially biased estimates in small samples (Alonso-Borrego and Arellano 1999; Blundell and Bond 1998), and (iii) exacerbating biases by decreasing the signal-to-noise ratio (Griliches and Hausman 1986).

Mostly, two main variants of the system panel estimator, one-step and two-step system-GMM, are preferred in econometric studies. While one-step system estimator assumes homoscedastic errors, two-step estimator constructs heteroscedasticity-consistent standard errors, and thus asymptotically accepted to be more efficient relative to the former (Arellano and Bond 1991). Nonetheless, two-step estimator becomes a poor guide for small samples that has large number of instruments, as it raises overfitting problem and may produce standard errors that are biased downwards, which is evident in most of the Monte Carlo experiments (Beck and Levine 2004:426). Due to this, we choose one-step system estimator and use robust standard errors as common in most studies.

The consistency of system-GMM estimator hinges on the validity of two main assumptions; (i) the error terms do not exhibit serial correlation, and (ii) the instruments must be valid. In addressing these issues, we use two common specification tests suggested by Arellano and Bond (1991), Arellano and Bover (1995), and Blundell and Bond (1998). The first is the Hansen test of over-identifying restrictions,[19] which tests the validity of instruments used in the regression.

[19] As we applied robust standard errors in each model, instead of Sargan test, Hansen test results are provided to address the validity of instruments.

Table 2.5: Islamic Banking and Human Development: Pooling and Fixed Effect Regressions

	Pooling Effect						Fixed Effect					
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
GDP per capita growth	-0,002	-0,0007	-0,0004	-0,0003	-0,0006	-0,0004	-0.0007**	-0,0004	-0,0004	-0,0004	-0,0004	-0,0004
	[0.0013]	[0.0011]	[0.0011]	[0.0011]	[0.0011]	[0.0011]	[0.0003]	[0.0004]	[0.0004]	[0.0004]	[0.0004]	[0.0004]
Trade openness	0.0005***	0.0003**	0,0002	0,0002	0.0003*	0,0002	0.0001	-0,0001	0.0001	-0,0001	0.0001	0.0001
	[0.0002]	[0.0002]	[0.0002]	[0.0002]	[0.0002]	[0.0002]	[0.0002]	[0.0003]	[0.0002]	[0.0003]	[0.0002]	[0.0002]
Oil rent	-0,0003	0.0009**	0,0006	0.0006*	0.0007*	0,0006	-0.0009**	-0.0008*	-0.0010*	-0.0008*	-0.0009*	-0.0009*
	[0.0004]	[0.0004]	[0.0004]	[0.0004]	[0.0004]	[0.0004]	[0.0004]	[0.0004]	[0.0005]	[0.0004]	[0.0005]	[0.0005]
Industrialisation	-0,0854	-0,051	-0,0644	-0,0561	-0,0608	-0,0561	0,2339	0,2385	0,292	0,2497	0,2647	0,2543
	[0.1256]	[0.1228]	[0.1274]	[0.1259]	[0.1265]	[0.1257]	[0.3963]	[0.3840]	[0.3774]	[0.3774]	[0.3731]	[0.3755]
Rule of law	0.0012***	0.0012***	0.0012***	0.0012***	0.0012***	0.0012***	0,0004	0,0003	0,0002	0,0002	0,0002	0,0002
	[0.0004]	[0.0004]	[0.0004]	[0.0003]	[0.0004]	[0.0004]	[0.0007]	[0.0007]	[0.0007]	[0.0007]	[0.0007]	[0.0007]
Political stability	0.0022***	0.0013***	0.0013***	0.0014***	0.0013***	0.0014***	-0,0006	-0,0005	-0,0004	-0,0004	-0,0004	-0,0004
	[0.0003]	[0.0003]	[0.0003]	[0.0003]	[0.0003]	[0.0003]	[0.0005]	[0.0004]	[0.0004]	[0.0004]	[0.0004]	[0.0005]
Overall banking development		0.0014***	0.0014***	0.0014***	0.0014***	0.0014***		0,0004	0,0004	0,0004	0,0004	0,0004
		[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]		[0.0003]	[0.0004]	[0.0004]	[0.0004]	[0.0004]
Financing by Islamic banks/GDP			0.1157**						0,0569			
			[0.0512]						[0.0488]			
Assets of Islamic banks/GDP				0.0681***						0,0161		
				[0.0158]						[0.0269]		
Deposits of Islamic banks/GDP					0,0539						0,0299	
					[0.0497]						[0.0275]	
Investments of Islamic banks/GDP						0.0853***						0,0262
						[0.0249]						[0.0317]
Constant	0.5509***	0.5024***	0.5055***	0.5057***	0.5038***	0.5059***	0.6770***	0.6641***	0.6566***	0.6609***	0.6602***	0.6603***
	[0.0228]	[0.0222]	[0.0224]	[0.0220]	[0.0225]	[0.0221]	[0.0675]	[0.0707]	[0.0677]	[0.0693]	[0.0684]	[0.0687]
N	252	252	252	252	252	252	252	252	252	252	252	252
R^2	0.556	0.669	0.677	0.683	0.671	0.680	0.109	0.139	0.154	0.144	0.149	0.147

The second test, AR2 test, examines whether error terms are serially correlated or not. Similarly, Wald test, known as F-test in small samples, examines the joint significance of whether two or more variables should be included in the regression jointly. The results of each test pose no problem of applying system-GMM and joint significance of variables. The values of Hansen and AR2 test results are given at the bottom of each table.

Table 2.6: Islamic Banking and Human Development: Dynamic Panel System-GMM Estimations

	(1)	(2)	(3)	(4)	(5)	(6)
GDP per capita growth	0,0001 [0.0001]	0,0001 [0.0001]	0,0002 [0.0001]	0,0002 [0.0002]	0,0001 [0.0002]	0,0002 [0.0001]
Trade openness	-0,0001 [0.0001]	0.0001 [0.0000]	-0.0001* [0.0000]	-0.0001* [0.0000]	-0,0001 [0.0000]	-0.0001* [0.0000]
Oil rent	0,0001 [0.0002]	0.0002* [0.0001]	0.0001* [0.0001]	0.0002* [0.0001]	0,0001 [0.0001]	0.0001* [0.0001]
Industrialisation	0.0436* [0.0228]	0.0378* [0.0205]	0.0387** [0.0186]	0.0422** [0.0177]	0.0389** [0.0181]	0.0412** [0.0171]
Rule of law	0.0001 [0.0001]	0,0001 [0.0001]	0,0001 [0.0001]	0,0001 [0.0001]	0,0001 [0.0001]	0,0001 [0.0001]
Political stability	-0,0001 [0.0001]	-0,0001 [0.0001]	-0,0001 [0.0001]	-0,0001 [0.0001]	-0,0001 [0.0001]	-0,0001 [0.0001]
Credit by deposit money banks to the private sector/GDP		0,0002 [0.0002]	0,0002 [0.0002]	0,0001 [0.0002]	0,0001 [0.0002]	0,0001 [0.0002]
Financing by Islamic banks/GDP			0,0101 [0.0078]			
Assets of Islamic banks/GDP				0,007 [0.0052]		
Deposits of Islamic banks/GDP					0,0083 [0.0098]	
Investments of Islamic banks/GDP						0,0093 [0.0067]
Constant	-0,0152 [0.0309]	0,0151 [0.0229]	0,0145 [0.0216]	0,0142 [0.0231]	0,0144 [0.0237]	0,0138 [0.0229]
Number of obs.	231	231	231	231	231	231
Hansen-prob.	0.373	0.168	0.181	0.133	0.151	0.122
AR2-prob.	0.672	0.633	0.621	0.744	0.677	0.708

Notes: Robust standard errors in brackets; * significant at 10%; ** significant at 5%; *** significant at 1%. AR(2): Arellano and Bond test of second order autocorrelation.

In applying the one-step system-GMM, the variables for overall financial development, Islamic banking growth, political stability and oil rent are treated as endogenous, and first and second lags of them are incorporated in the regression model. Theoretical and practical considerations, mentioned in the literature review, suggest treating GDP per capita growth, trade openness, industrialisation and rule of law as exogenous variables.

Table 2.6 presents the findings of system-GMM estimator. In parallel with the fixed effect model, the results suggest that Islamic banking growth has insignificant effect on economic development in all of the four different regression models with the coefficients ranging between 0,007 and 0,01. This ensures that the transactional growth in Islamic banking sector observed throughout the decades could hardly bring about transformational achievement in the development processes of countries. In other words, the expansion and growth of Islamic banking sector in the financial system through its assets, deposits and investments has long way to generate developmentalist outcomes. It should be noted that in such a conclusion, the present relatively small size of Islamic banking sector within the national financial systems of the sampled countries has been considered.

As depicted in Table 2.6, the overall banking growth, likewise, has no significant effect on HDI which is in parallel with our theoretical explanations. Since conventional banking system can hardly go beyond debt-based mechanism by concentrating on credit financing in developing countries and their fragile economies, sharing and participation dimensions of developmentalism in investment activities have been sacrificed to get exorbitant profits through creating riskless debt. In a more sophisticated way, it is apparent that conventional banking system is a product of capitalist economic system, which is transformed into a particular form, in its recent history, through a substantial pattern of financialisation. As part of the objective of creating financialised economy, conventional banks serve mainly for monopolistic multinational corporations (MNCs) to provide fund for their investment activities so that capital accumulation process is maintained within particular financial ways. The entire operations of such an economy is called as ‘monopolised capitalist economy’ (Foster 2007:3) wherein a huge amount of surplus is created by a very few number of MNCs. Capital, in such forms of economic systems, functions as speculative pursuit instead of long-term investment projects in the real economy. Therefore, there is no longer a direct connection between productive investment and financial assets. As such, societal implications of conventional banking assets bring adverse effects, since it contributes in making of a ‘casino society’, a term that was used first by Bianco (1985:78).

While fixed effect results suggest weak significance of a negative impact of GDP per capita growth on HDI, it now turns out to show insignificant but positive results in system-GMM results. This finding is surprising for most of the empirical researchers, because it is a rule of thumb in growth studies that a rise in GDP per capita should infer fostering economic growth. However, by taking into account the distribution issue, we expect such an inverse or weak positive relationship between GDP per capita growth and HDI, mainly for the countries in which an increase in total GDP exacerbates the income distribution gap through benefiting rich while leaving the poor unaffected or negatively affected. That means a good income smoothing is imprisoned in the abstract mathematical calculations rather than reflecting the real performance.

This result necessitates re-examining the contemporary function of GDP and its historical evolution towards being an irrevocable benchmark for economic growth studies that aim to provide some evidences for economic wellbeing and social welfare. Accordingly, one must say that the very concept of GDP is a product of market-oriented thinking (Sandel 2012), which assumes all goods and services in an economy to be commensurable and translated into a particular measure. Therefore, its proponents claim that GDP is able to measure wellbeing or welfare. However, in fact, GDP does not mean anything beyond national income, as it is a made-up entity that dates back only to 1940s and constructed from an ambition of measuring national output during wartimes, since financing warfare was the motivation for GDP to rise in order to measure productive capacity to use scarce resources and labour in a most efficient way (Coyle 2014:9). Thus, GDP has never been intended to measure wellbeing and social welfare in a historical sense; for it naturally does not consider the consequences of economic growth. To give an example, the proliferation of scientific activities and technological process between 1940s and 1970s accompanied with a substantial increase in GDP; however, at the same period, the world was suffering from various socioeconomic problems including social revolts, protests and student movements, anarchy and conflict all around the world during the period in question. This means that wellbeing is not perfectly correlated with GDP per capita, as the consequences matter in shaping its boundaries.

The role of trade openness in fuelling economic development does not meet the expectations due to its small but negatively significant effect. Thus, the implications of open trade in the sampled countries are in contradiction with the assumptions of neoclassical economics, which stipulates trade liberalisation for economic progress and hence essentialises free-market understanding derived from *laissez-faire* ideology. On the contrary, the findings match up with the Wallersteinan understanding of centre-periphery relations (Wallerstein 1974) in which open trade is considered to be in favour of developed countries at the expense of impoverishing the rest. Therefore, global expansion of trade activities is accompanied with an adverse effect on development process of domestic economy.

The influence of oil rent on economic development is somewhat contested issue, since, on the one hand, oil rich countries take advantage of its rent and inflow of petrodollars; while on the other hand, the lack of appropriate channels or desire to direct oil money into investable areas annihilates its potential to step those counties forward. In this circumstance, the future of oil rich countries, especially GCC region, hinges on the ways to reduce dependency to oil income and create, instead, knowledge-based economy understanding (*see*: Peterson 2009; Weber 2011). However, oil rich countries today do not display, in general, productive economies, rather they inefficiently consume their sources and enjoy the advantages of oil richness amongst few riches. In recognition of this, system-GMM results suggest a poor but positive impact of oil rent over economic development. This is meaningful in the sense that the great potential of oil in expanding the frontiers of economic wealth is not fully realised due to political economy factors in oil rich countries such as the monopoly of oil revenue in the hands of few royal families; thereby, it only demonstrates a side effect over society, as shown in the coefficient of 0.01 and 0.02% in Table 2.6.

As the results depicts in Table 2.6, industrialisation matters for economic development in all models, implying that the real economy side - especially manufacturing - should be strengthened to achieve welfare and prosperity in the national level. The coefficients in each model ranging between 3% and 4% evidences that the most contributing dimension of economic development comes from industrial development.

The political economy factors, rule of law and political stability, do not seem to affect economic development significantly. Drawing special attention on it, political stability has a weak negative relationship with HDI based on the all models in Table 2.6. This can be interpreted in a way that either authoritarian or democratic regimes in the observed countries are unable to advance human development. Thus, this result suggests that redistributive justice mechanism must be located in the sample countries through reform or destabilisation in political sphere, which hence necessitates redistribution of political power.

In crystalizing the nexus between Islamic banking growth and economic development, system-GMM results imply that Islamic banking and finance has still a long-time to grow and expand, and, therefore, it should recourse to the developmentalist objectives in its development trajectory identified by founding fathers of Islamic economics as signified by IME by operating within a system based on real asset backed financing and risk sharing nature rather than mimicking conventional financial system.

2.5.3.3. Robustness analysis and alternative specifications: testing different variables for overall financial development

After using different variables for Islamic banking growth to evidence to what extent the results are robust to the alterations in the conditioning information set and different variables, in this section, alternative measures for overall financial development is employed and the impact of Islamic banking growth on economic development - with the same indicators - is examined empirically. As the results in Table 2.7 demonstrates, in the first three model, private credit by bank and other financial institutions to GDP is used as an indicator for overall financial development instead of previously used private credit by deposit money banks to GDP. When the overall financial development is controlled for, Islamic banking growth variables show no difference with the previous results and indicates an insignificant impact on economic development. These three models show more or less the same results with the results in Table 2.6. However, the rule of law turns out to have positive and significant effect in the first and third models.

Model 4 and model 5 measures development of both Islamic banking and conventional financial system respectively by their asset and deposit size. Not differently, these two variables remain insignificant, and other variables and their statistical significance levels mostly do not alter. These results suggest once again that Islamic banks should reconsider its potential contributions to developmentalist objectives by giving more emphasis on risk and profit-loss sharing instruments so that the optimality between social and financial performance is established.

Table 2.7: Alternative Variables for Overall Financial Development: System GMM Estimations

	(1)	(2)	(3)	(4)	(5)
GDP per capita	0,0001	0,0001	0,0001	0,0002	0.0001
	[0.0002]	[0.0002]	[0.0002]	[0.0001]	[0.0002]
Trade openness	-0.0000**	-0.0000*	-0.0001**	-0,0001	0.0001
	[0.0000]	[0.0000]	[0.0000]	[0.0001]	[0.0000]
Oil rent	0.0002*	0.0002**	0.0002*	0,0001	0.0003*
	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]
Industrialisation	0.0428***	0.0452***	0.0442***	0.0546*	0.0717**
	[0.0137]	[0.0141]	[0.0127]	[0.0300]	[0.0326]
Rule of law	0.0002*	0,0001	0,0001	0.0001	0.0002*
	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]
Political stability	-0,0001	-0,0001	-0,0001	0.0001	-0,0001
	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]
Overall financial development	0,0001	0,0001	0,0001		
	[0.0001]	[0.0001]	[0.0001]		
Financing by Islamic banks/GDP	0,0068				
	[0.0089]				
Assets of Islamic banks/GDP		0,0021		0,0071	
		[0.0077]		[0.0072]	
Deposits of Islamic banks/GDP			0,0031		0,0067
			[0.0050]		[0.0049]
Financial system assets/GDP				0.0001	
				[0.0001]	
Financial system deposits/GDP					0,0001
					[0.0001]
Constant	0,0161	0,0162	0,0133	-0,0141	0,0216
	[0.0201]	[0.0246]	[0.0215]	[0.0200]	[0.0261]
N	231	231	231	231	231
Hansen-prob.	0.111	0.107	0.080	0.110	0.201
AR2-prob.	0.524	0.555	0.550	0.959	0.586

Notes: Robust standard errors in brackets; * significant at 10%; ** significant at 5%; *** significant at 1%. AR(2): Arellano and Bond test of second order autocorrelation.

2.5.3.4. Sensitivity analysis

Further to conducting robustness analysis through alternative measures, conducted first with the variables of Islamic banking growth, and then that of overall financial development, Table 2.8 illustrates sensitivity analysis based on the change in sample composition through the share of Muslim population above 50%[20] and 65%[21], and net oil exporter countries[22]. By doing so, it would be possible to assess whether the effect of Islamic banking on economic development substantially differ in countries with high share of Muslim population. In addition, another regression was undertaken by sampling only net oil exporter countries to empirically examine if Islamic banks perform relatively better in oil rich countries. In the case that the results confirm such a significance, then we would infer that oil money helps contributing economic development through their efficient use by Islamic banks.

The first sample is constructed by considering those countries that have more than 50% Muslim population share, while in the second sample the percentage was increased to 65%. In both regression results as depicted in Table 2.8, Islamic banking growth, overall financial development and trade liberalisation present no significance over HDI, whereas GDP per capita, oil rent and industrialisation imply positive effect at least 1% significance level. Interestingly, political economy factors become an important determinant of economic development in the sample constructed by the condition of Muslim population share above 65%. It should be noted that the signs of each variable are in line with our theoretical premises. Lastly, regression results, by using the sample constructed with the net oil importer countries, suggest that industrialisation and oil rent do matter for economic development, whilst the rest of variables are far from fuelling development trajectories of countries.

2.6. CONCLUSION

The entire debate on finance-growth nexus enriched with the explorations of empirical studies surfaces the inferiority of mainstream approach towards human wellbeing, growth and development issues particularly in a world where finance is drastically being disembedded from economy (the bifurcation of finance and economy). As the incontestable prevalence of

[20] After applying this condition, we excluded Bosnia, South Africa and the United Kingdom from the dataset, and hence number of countries decreased to 18. Also, as the sample size decreases, we only used the first lag of endogenous variables since, otherwise, the number of instruments were exceeding the number of groups.
[21] Here, we had to make further exclusions of Lebanon and Malaysia in addition to Bosnia, South Africa and the United Kingdom. Therefore, we only had 16 countries in the cross-section data. Similarly, the first lags are taken into account for the endogenous variables.
[22] As mentioned before, the structure of robustness analyses is inspired by the work of Imam & Kpodar (2016).

growth concept against development is evident in the theoretical discussions and empirical studies, almost every discursive study and quantitatively empirical research refer to growth in order to elucidate the impact of finance-related institutional and non-institutional effects on individual, society and whole economy.

In a similar vein, with the evolvement of economies into a heavy financialisation pattern which necessarily accompanies with a substantial change in the goal of economic activities, the role of finance has been sacralised in accomplishing the exigencies of economic growth with a basic motivation of establishing finance-intensive policies of economic development.

However, finance has no longer been deemed to reveal developmentalist consequences through improving individual's capabilities and functions, and necessarily enhancing economic performance, but the aim with the financialisation process is rather to employ an opportunity space, independent from the objectives above, where various incumbents, pressure groups and rent seekers aim to financiate and commodificate values and things through various financial institutions (multinational companies, stock markets, banks and *etc*.) and instruments, whereby these can be sold in the market as a commodity which allows for the interest groups to make private gains from them.

Through comprehension of the substantiation of finance-growth nexus subrogating developmentalist objectives, it becomes clear why financial development and its impacts on socioeconomic life are narrowly dealt by mainstream economists with such indicators of capital, savings, investment, technology and so on. These indicators incommensurately show one side of the coin which explains finance-based economic growth models irrespective of touching upon social, political and cultural dimensions of economic activities. A distinction between growth and development, hence, is not subject to extensive concern from a conventional point of view in regard to effects of finance on different aspects of life. The utmost concern is the growth of investment activities and the proliferation of capital as reflected through the idea of 'capital fundamentalism' (King and Levine 1994), so that finance would become more widespread all over the world, which consecutively leads to spurn developmentalist aims of economic activities.

Table 2.8: Sensitivity Analysis: Change in Sample Composition (System GMM Estimations)

	Muslim population share above 50%			Muslim population share above 65%			Net oil exporter countries		
	(1)	(2)	(3)	(1)	(2)	(3)	(1)	(2)	(3)
GDP per capita	0.0002*	0.0003**	0.0002*	0.0002*	0.0002**	0,0002	0,0001	0,0002	0,0001
	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]
Trade openness	0.0001	0.0001	0.0001	0.0001	0.0001	0.0001	-0.0000*	-0.0001*	0.0001
	[0.0000]	[0.0000]	[0.0001]	[0.0000]	[0.0000]	[0.0000]	[0.0000]	[0.0000]	[0.0000]
Oil rent	0,0001	0.0003*	0,0001	0.0001*	0.0002**	0.0001**	0.0003**	0.0003***	0.0004***
	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]
Industrialisation	0.0745**	0.0758***	0.0723**	0,0415	0.0431*	0,0441	0.0711***	0.0722***	0.0731***
	[0.0305]	[0.0283]	[0.0320]	[0.0344]	[0.0254]	[0.0300]	[0.0196]	[0.0198]	[0.0197]
Rule of law	0.0001	0.0001	0.0001	0,0001	0.0001**	0.0001**	0,0001	0.0001	0,0001
	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]
Political stability	-0.0002*	-0,0001	-0,0002	-0.0001**	-0.0002**	-0.0002***	-0,0001	-0,0001	-0,0002
	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]
Overall financial development	-0,0003	-0,0001	-0,0003	-0,0001	0.0001	-0,0001	0.0001	0.0001	0.0001
	[0.0002]	[0.0001]	[0.0002]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]	[0.0001]
Financing by Islamic banks/GDP	0,0212			0,0067			0,0249		
	[0.0144]			[0.0070]			[0.0176]		
Assets of Islamic banks/GDP		0,0071			0,0006			0,0214	
		[0.0085]			[0.0039]			[0.0250]	
Deposits of Islamic banks/GDP			0,01			0,0031			0,0096
			[0.0082]			[0.0029]			[0.0094]
Constant	-0,0353	-0,0264	-0,0384	-0,0111	-0,006	-0,0091	-0,004	-0,0108	0,0021
	[0.0356]	[0.0277]	[0.0348]	[0.0122]	[0.0108]	[0.0093]	[0.0167]	[0.0189]	[0.0146]
N	198	198	198	176	176	176	176	176	176
Hansen-prob.	0.234	0.220	0.312	0.172	0.097	0.123	0.476	0.458	0.405
AR2-prob.	0.576	0.718	0.611	0.827	0.844	0.852	0.653	0.606	0.714

Note: Robust standard errors in brackets; * significant at 10%; ** significant at 5%; *** significant at 1%. AR(2): Arellano and Bond test of second order autocorrelation.

Beyond growth orientedness, development reflecting the dynamic analysis above transcends economic considerations and stimulates a substantial change in the existing functioning of economic, social, legal and political institutions. In this manner, as IME envisages, development can be defined as a continuous process which paves the way for an equilibrium amongst improvements in different structures (social, economic, political, cultural and *etc.*) through the embedment of morality at the core of whole development agenda, so that any potentially contradictory situation between these structures is nipped in the bud by the moral mechanism. This approach necessitates that financial structure of an economy should be substantiated with the above-defined developmentalist perspective, which also reflects the aspirations of Islamic developmentalism, as *rububiyah* and *tazkiyah* concepts essentialise development as a core objective within emancipation and empowerment objectives of Islam. Thus, finance-development nexus, which is essential to be explored from this point of view, has barely been undertaken in conventional and heterodox economic systems in a systematic manner. What have already been studied extensively in the entire literature is finance-growth nexus as response to the basic question about the role of finance on the development of human, society and economy; therefore, hardly any study has attempted to 'go beyond the box' in delving into 'finance-development nexus', which, hence, has created a significant gap in the mentioned literature.

This study argues that Islamic finance industry has experienced a similar transformation in its objectives through the influences of conventional theoretical underpinnings and practices of financing, although the emergence and existence of Islamic finance initially relates to 'developmentalist' objectives and 'substantive morality' of IME as advanced, in a modern meaning, since 1960s. This argument is evidenced empirically by examining the relationship between Islamic banking growth and economic development; accordingly, the results show that Islamic banking has no significant impact on human development standing far away from developmentalist trajectories of countries, albeit founding fathers of Islamic economics institutionalised Islamic banking to serve for both financial and social development harmonically as *tazkiyah* axiom suggests. As Islamic finance could not fulfil such an objective due to the gradual convergence towards mainstream finance, it must be concluded that as long as Islamic finance mimics the conventional financialisation trend, empirical studies that examine Islamic banking-development nexus would not have any implications other than stating the failure and evidencing this through different estimation models.

This study, therefore, aims to fill this gap by incorporating Islamic developmentalism into the debate within expanding and growing Islamic finance. By the same token, it suggests a re-examination of the role of Islamic finance on economic, social, legal and political structures through breaking the finance-growth link and offering a finance-development relationship instead, through which financialisation is avoided by considering 'financing' as part of embeddedness. This study, hence, aims to think 'beyond the box' by essentialising an embedded nature of finance through developmentalism in the form of human well-being instead of considering and stigmatising everything around us as 'capital' (such as 'human capital', 'social capital', 'intellectual capital' *etc*.). This neo-classical fallacy of re-constructing everything as 'capital' is not considered to be the frame of analysis in this study, as it aims to deconstruct the notion of 'capital' being attributed as the source of 'growth and development'; and therefore, aims to use 'moral economy frame' to assess the 'financing and development'.

As opposed to such an imagination, in the current practice, IBF favours capital domination within Islamic banks as evidenced in its operational areas including modes of finance, sectorial distribution of financing, and governance structure. For this reason, Islamic banks has never brought about momentous changes in development trajectories of countries wherein they keep operating. The *ihsani* process, essentialised in Islamic developmentalism, is not addressed in the Islamic financial area as a profit and loss sharing activity, but rather individualist and self-maximisation motives have taken place at the core of financial transactions. Thus, self-development has never been accompanied with societal development. In this manner, for instance, Islamic banks intensify their financing modes on fictitious products that resemble conventional financial transactions, such as the case with organised *tawarruq*, which is considered to be both un-lawful and immoral as the *fatwa* of International *Fiqh* Academy of OIC states but practised by Islamic banks under market pressure and capital efficiency. In a similar manner, in the corporate level, Islamic banks' shareholder value-oriented governance structure is at odds with the ideal Islamic corporate governance, as the statistical records measured for shareholder value orientation evidence.

These examples explicitly demonstrate that market system and price mechanism push its own self-regulated nature on Islamic finance and shape its current and future practices not to diverge from capital-oriented activities of finance whereby it gains global recognition. More broadly, Islamic finance is kept within the boundaries of old norms shaped by capital predominance, and hence it is not allowed to constitute an alternative to the prevailing financial system by submitting to the established capital forms and norms rather than re-defining capital as Islamic economics suggests. However, as Islamic developmentalism suggests, Islamic finance would emerge as a bottom-up demand from society to meet financial needs of individuals under a simple but functional role of 'financing' *vis-à-vis* a self-proclaimed 'finance' understanding constructed by mainstream economics. Nevertheless, it could not position itself within a moral economy understanding and has always targeted to shine out as an alternative market segment within global financial system. The gradual process of diverging from moral economy perspective is elucidated through historical facts and conditions of Muslim world surrounded by a new regulation of world financial system in the post-war period. In this sense, Islamic banks borrowed the existing regulations and standards of mainstream financial system to apply over their banking system such as (LIBOR); thereby, it was implicitly accepted that the challenges in legal issues, risk natures and operational model can be resolved through conventional prescriptions.

The next chapter, accordingly, expands the scope of non-developmental or financial expansion of Islamic finance and its capital fundamentalism through the introduction of the notion of Islamic financialisation, which has barely been associated in the literature of Islamic economics due to an unwitting negligence of the term by practitioners and theoreticians. Therefore, it argues that the social failure roots in, to a large extent, the adopted financial logic borrowed from mainstream economics whereby the utmost importance is given to financial sector to take place and substantialise at the core of economic activities. In evidencing Islamic financialisation, the chapter also conducts some econometric analysis whereby Islamic financial operations are examined thoroughly.

In furthering and crystallising the debate, Chapter 4 associates the elaborated challenges and failures of Islamic finance with methodological obscurity in defining the objectives of Islamic economics. In other words, both developmentalist failure of Islamic finance and the financialisation process ascertained that the initial concern with theory making should be on methodological issues, for knowledge can only be authenticated through a rigorous methodology. Considering *maqasid al-Shari'ah* as the methodological base of Islamic economics and finance, Chapter 4 identifies that the observed developmentalist challenges as evidenced in this study relates also the way *maqasid al-Shari'ah* is considered and interpreted by academics, practitioners as well as *Shari'ah* scholars in IBF. In search for addressing methodological dimension, in a response, hence, Chapter 4 develops its proactive *maqasid al-Shari'ah* framework as the essential methodology of Islamic economics so that the consequences of IBF can be moderated in favour of economic and social development, as even the conventional banks and financial institutions are given the task of fulfilling SDGs.

CHAPTER 3

FINANCIALISATION AND DISEMBEDDEDNESS IN ISLAMIC BANKING: CRITICAL DISCOURSE AND EMPIRICAL ANALYSES ON PERFORMING BANKING AND FINANCE *VS.* ISLAMIC MORAL ECONOMY

3.1. INTRODUCTION

Islamic finance, as the phrase implies, embraces a peculiar mode of finance which grounds its theoretical underpinnings to Islamic economics paradigm, and hence, operates within the ambit of Islamic legal rules and moral obligations. As can be inferred, it is motivated by religious concern of facilitating an exclusive financial system that is constructed by Islamic principles, values and norms. Contrary to the interest-based nature of global financial system through which exorbitant profits are realised at the expense of impoverishing rest of the world, IFIs aim to circumvent social imbalance triggered by interest issue in their original imaginations – as *Qur'an* (2: 278-9) prohibits *riba* (interest) – by positing 'profit and loss sharing' and 'risk-sharing' operations of financing within the umbrella of 'sharing and participatory economy' paradigm.

3.1.1. Problem Statement

Established four decades ago and proliferated in a short span of time across the globe, Islamic finance, at its state of art, is extolled for its performance to show an unprecedented success in achieving a continuous growth in terms of asset size, and for its financial services reaching an overall total value of US$1.893 trillion as of 2016 (Islamic Financial Services Board (IFSB) 2017:7). Despite the share of Islamic financial assets ($1.893 trillion) remains only 1% of the global financial market of US$127 trillion (Ernst and Young (E&Y) 2016), Islamic Financial Institutions (henceforth, IFIs) are increasingly becoming part and parcel of the global financial system. This, in return, leads to the expectation that the momentum gained with Islamic finance should accompany with economic wellbeing across its operating fields due to the fact that financial development would necessarily foster economic growth (see: King and Levine 1993;

Demetriades and Luintel 1996; Rousseau and Wachtel 1998; Beck, Georgiadis and Straub 2014 amongst others) and generate economic and social welfare in a wider sense.

While Islamic finance secures its position in the global financial order by introducing new products and permeating through untapped fields, its distinguishing feature of being a religion-based model –rather than self-regulated market system- engenders some challenges in integrating into global, secular, modern and capitalistic characteristics of mainstream finance. This is due to the reason that Islam attaches certain principles to financial activities such as prohibitions of *riba* (interest), *gharar* (excessive uncertainty) and *maysir* (gambling), whereas conventional financial markets trust self-regulation without reliance on divine knowledge to lead its activities. This obliges Islamic finance scholars to adopt either an authentic but necessarily non-globalised financial system within the boundaries of Islamic law, or a hybrid system that mimics conventional finance but renders relatively more efficient performance with its quite often questionable activities in terms of conforming to the essence of Islamic legal and moral rulings.

Remembering ethical principles embedded in its foundational premises, Islamic finance also aims to reveal developmentalist consequences in the form of social good in such a challenging atmosphere. Developmentalism as a social objective in financial activities of Muslim societies was mainly essentialised by the founding fathers of Islamic economics, who considered Islamic finance to be ethically driven industry that has to exhibit thriving 'social performance' by 'contributing to development' as well as financial performance (see: Mannan 1970; Chapra 1979; Zarqa 1980; Siddiqi 1981; Choudhury 1986; Ahmad 1994; Naqvi 2003 amongst others).

Examining at its economic outlook within its experiment over the last forty years, it can be somewhat asserted that IFIs are financially performing moderate (Hassan and Aliyu 2018); however, while developmentalist contributions are reckoned with, they lag far behind the aspired level and failed to accommodate social performance. The observed developmentalist failure is evidenced in the previous chapter (Chapter 2), where an empirical analysis on whether Islamic banking contributes to economic development patterns in selected Muslim dominated countries is presented. By selecting Human Development Index (HDI) as the proxy for economic development, and the total financing and total asset values of selected Islamic banks, as opposed to the expectations and aspirations, the study concluded that Islamic banking has poor contributions to economic development trajectories of the sampled countries. Such a poor social and developmentalist contribution or weak transformational performance is labelled as 'social failure' in relation to the aspirations, while the current practice is conceptualised as 'the second-best solution' (Asutay 2012, 2007b). This study relates the observed social failure of Islamic banks (IBs) to and argues that one of the sources of such a failure is the 'financialisation' phenomenon in the sense of centring 'finance' in the form of 'financial' in economic activities.

As a flourishing conceptualisation - of the practice of the historical trajectory of finance - in the heterodox literature, financialisation represents a systemic transformation of capitalist economies during the last few decades that brought about a sharp divergence between economic and financial activities in favour of booming finance in the face of performing productive economy as part of the shift towards finance-led capitalism. As the idea of Islamic economics burgeoned at this stage of capitalist world system, this study argues that Islamic finance emerged as a product of post-colonial discourse through negotiation between religion and finance, the trajectory of which has, however, been shaped with the inspiration from financialisation phenomenon resulting into convergence.

Financialisation of Islamic finance, therefore, represents the significant rise of modern debt-based Islamic financial instruments within the real sector, which dilute risk and profit-loss sharing objectives of Islamic finance significantly and has scarce impact on productive aspects of economy. It may seem misleading at first that there should not be a clear delinking of finance from economy in the case of Islamic finance due to its asset-backed feature that implies having strong ties with the real sector. However, in fact, the asset-backed characteristic is used instrumentally to appear within the frontiers of *Shari'ah* compliant financial activities. Thus, the consequential aspects of modern debt-based Islamic financial transactions show broad affinities with conventional financial system. The difference between conventional and Islamic financialisation, hence, emerges out of the impossibility of a total elimination of asset-backed feature of Islamic finance due to *Shari'ah* considerations, albeit this feature has limited implications for productive economy. Once the consequence-oriented evaluation is adopted, most applications of debt-based instruments such as *murabahah*, *tawarruq* and *sukuk* should be reconsidered in light of their long-run impacts on economy and society. For instance, while, on the one hand, *murabahah* relates to the real economy through financing consumer durables, the long-run impacts would be the proliferation of debt within the economy that resembles the experience in the Western countries in terms of giving rise to devastating crisis whereby IFIs yield the same financialisation consequence as conventional finance.

Based on such a positioning, one cannot expect developmentalist objectives from IFIs in an environment of financialised economy, for financialisation is itself a project of eliminating human element in economic relations through submerging human interaction in a nexus of financial relations, which enunciates the dominance and power of capital over other stakeholders, while *riba* prohibition refers to questioning the overwhelming hegemony of capital over other stakeholders including human (Asutay 2018). Therefore, Polanyi (1944), considers the emergence of social protections movements as rescuing human, land, labour and capital, which has recently been echoed by Pope Francis (2015) in his call for ending hegemony of techno-economic paradigm to free human. This research, hence, aims at developing a critical perspective on Islamic finance through the lens of political economy of financialisation to explore as to how Islamic finance has converged towards financialisation objective away from Islamic aspirational claims of authenticity.

3.1.2. Aims, Objectives and Research Questions

In an attempt to develop a critical discourse analysis on the notion of financialisation from the Islamic Political Economy perspective and substantiate it with some empirical evidence, this study aims to reconsider both achievements and social failure of Islamic finance under the context of 'financialisation of Islamic finance', and hence reorient entire debate into political economy realm. It is argued, hence, that the emergence and systematic institutionalisation of modern Islamic finance industry in 1960s was not a coincidental development, but rather highly influenced from the essentialisation of finance dominated economic system (amongst the studies emphasising political economy aspects of Islamic finance and its relationship with finance-dominated global economic system, *see*: Pollard and Samers 2007; Azarian 2011; Rethel 2011; Mohamad and Saravanamuttu 2015; Hoggarth 2016). Thus, Islamic finance could only become an in-paradigm alternative within debt-based economic environment. This chapter, therefore, aims to challenge the observed and developing Islamic financialisation as an attempt that it is invariably fictitious in nature and is a government-led top-down process in most of the countries where Islamic finance is visible, rather than an outcome of bottom-up demand for Islamic social services.

Along with this, it suggests an Islamic Political Economy approach to financialisation through which the nature, evolvement and burdens of financialised economies together with its implications on individual and social life are reconsidered in the light of Islamic ontology and epistemology. Accordingly, it deploys a critical discourse analysis on financialisation within Islamic Political Economy frame by giving particular attention to the exploration of Islamic financialisation.[23] In doing so, Polanyian understanding of embeddedness is adopted to address how Islamic financialisation impacts on social formation of Muslim societies by creating commodification and disembedment through Islamic finance operations.

Upon elaborating the theoretical construction of Islamic financialisation and its discursive analysis in a comprehensive manner, subsequently, an empirical analysis is conducted by examining the practical aspects of Islamic finance as a financialising activity within Islamic economics paradigm. Thus, the empirical part evidences as to how Islamic finance engenders a financialised view of (Islamic) economics through its operations. Specifically, it examines the impact of the ascendance of Islamic finance on financialisation trajectory of entire economy, with a panel of 14 Muslim-dominated countries covering the period of 2002-2014, to ascertain whether operations of Islamic finance, by and large, strengthen real economy or contribute to further financialisation in economies where domestic market share of Islamic finance reaches medium or high systematic importance. Accordingly, it employs a quantitative methodology in the second half of the research and makes use of secondary data with an unbalanced panel data analysis. A range of econometric techniques are utilised including pooled OLS, random effect and system-GMM estimators to address heterogeneity, over-identification and endogeneity issues.

In line with the aims and objectives of this study, following research questions are developed:

RQ_1: What are the historical dynamics behind the emergence of Islamic finance as a hybrid financial product and institution instead of an authentic alternative to global financial system?

RQ_2: In what sense does Islamic finance fail to operate beyond market economy understanding and becomes invariably disembedded and financialising economic practice?

RQ_3: What are the theoretical boundaries and scope of Islamic financialisation?

RQ_4: What are the institutional and practical implications of Islamic financialisation?

RQ_5: To what extent Islamic banking has contributed to financialisation in the countries where it has certain presence?

[23] In this study reference to 'Islamic financialisation' should not be understood in the form of Islam suggesting or resulting into 'financialisation. This simply means 'financialisation of Islamic banks and financial institutions'. However, in order to prevent the usage of definition (financialisation of Islamic banks/financial institutions), in this chapter occasionally the term 'Islamic financialisation' is used instead of 'financialisation of Islamic finance'.

While the study aims to respond to these research questions, the rest of the chapter is organised as follow: Section 3.2 presents a foundational ground on the concept of financialisation by exploring its emergence and historical development through shedding light on the political economy atmosphere of the 20^{th} century. Section 3.3 elaborates different approaches towards financialisation consisting of mainstream and heterodox economics understandings. Section 3.6 develops a moral economy approach upon financialisation phenomenon by examining Islamic finance industry in particular. However, before doing this, it necessarily addresses the nature, function and dimensions of moral economy understanding in Section 3.4, while the historical evolution, identity formation, substantive morality and the crosschecking system of Islamic moral economy is dissected in Section 3.5. After debating financialisation of Islamic finance in theoretical manner, an econometric analysis is conducted in Section 3.7 to examine whether theoretical argument is evidenced by econometric application.

3.2. FINANCIALISATION: A CONCEPTUAL EXPLORATION AND HISTORICAL TRAJECTORY OF ITS EMERGENCE

It is evident in the mainstream literature that the concept of financialisation had drawn little attention amongst academics until the 2007 global financial crisis. Heterodox economists, on the other hand, have explored and examined the concept more intimately, though still limited, for decades by considering the significantly rising share of finance in the whole economic activities to be a besetting factor against social justice, equity and development. While, in the aftermath of the crisis, mainstream economic theorists have hardly recognised the devastating effects and predatory character of financialisation, political economy theorists, economic sociologists and other schools of thoughts put more attention on the phenomenon and made significant contributions to crystallise the dangers of finance-led projects of economic growth. The literature on financialisation, hence, is slowly but substantially expanding with such contributions.

In this section, firstly, a brief overview about economic and political developments in the last century is discussed to contextualise the shift in the economic activities by the emerging dominance of financial activities and its movement towards the centre of economic operations. Then, acknowledging the historical roots of financialisation, the emergence and ascendance of the concept, multifarious definitions and approaches towards financialisation, key institutional players of financialisation, and its detrimental effects are addressed with a critical perspective.

3.2.1. The Way towards Financialisation

In the last century, some concepts have been widely propounded to describe certain transformations and shifts that took place in the recent history of the world. As such, globalisation, internationalisation, neoliberalism, post-colonialism – and many others having at the end of the word '-ism' or '-ation' as suffix – point out a particular series of evolutionary or direct changes in patterns, habits and functioning of individuals, institutions and society in general. Financialisation is such a term used to describe roughly somehow the profound rise of finance in the gravity of economic activities. In a more sophisticated way, financialisation signifies the transformation of mature capitalist economies into a new direction. In order to elaborate more on the concept, it is essential first to explore the economic and political environment in which financialisation has emerged and has been permeating through different spheres during the last few decades.

Resting on the Enlightenment philosophy, mainstream economic understanding, namely neo-classical economics, in the 20th century pursues the premises of positivist rationality and materialist worldview rejecting all metaphysical ideas and approaches by massing them in the basket of 'superstition' resulting into withering of religious knowledge and also ethical positioning.[24] In this regard, it relies on market mechanism to function as a social institution that regulates and determines the whole process of production, distribution and exchange. Besides, market system is conceived to function as the principal subject of fulfilling common good or public interest. Thus, both political and economic institutions are designed to be subservient to the idealised markets. The historical rise of finance in the 20th century represents this logic of idealised markets, as discussed in detail in the following sections.

3.2.1.1. The post-war boom

If the overall trajectory of the ascendance of finance is split into periods, the first period should last from the World War II to the 1970s, while the second period is still proceeding for the last four decades. The first phase of the financialisation process is termed multifariously, such as 'the thirty golden years' (Dembinski 2009), 'the era of Fordism' (Boyer 2000) or 'the post-war boom' (Tauss 2012). In concomitance with the end of the war, a new way of organising economic and social relations is adopted in this period that is characterised by the Fordist model of accumulation, the Keynesian welfare state and the Bretton woods system (Tauss 2012:54).

[24] For an extensive approach towards neoliberal economics and its reconceptualization of ethics and well-being, see the works of Sen (1985, 1990, 1993).

Fordism, originating in the US, basically introduced new production methods to increase productivity and efficiency (Holman 1993:221). However, not limited with the economic aspect, it has had impact of reorganising the society by imposing the American consumption model and lifestyle (Dembinski 2009:15) on the 'rest' through the booming new technical and cultural innovations such as mass motorisation, the aircraft industry, new media of mass communication (TV and radio), the markets for mass consumer durables (washing machines, refrigerators *etc.*) (Deutschmann 2011:377).

Together with the Fordist model, Keynesian welfare state policies fostered Europe's industrial growth that was once interrupted by the war. These policies, further, brought along low unemployment though inflation was rising, relative increase in real mass income, and notable decrease in income inequality compared to the period between wars (Phillips 2002). Along with the improvement and expansion of the higher education, a number of developments were observed in the conditions of working class. Due to the paid employment becoming widespread and rising standard of living, working class became aware of 'cultural embourgeoisement' (*see*: Bulmer 2016; Goldthorpe, Lockwood, Bechhofer, and Platt 1968). As the international labour markets were developing, career opportunities in international institutions emerged; which in return, provided a chance for social mobility from working class into the new middle class (Breen 2004).

The Bretton Woods system, on the other hand, was established as an institutional framework for the post-war world economy. Its main function was to provide a particular monetary and regulatory framework for the world economies as an intergovernmental system. This framework aimed to develop international trade mechanism through gradually reducing trade barriers, provide the convertibility of the US dollar into gold at $35 to the ounce, hence allowing for a currency system based on fixed exchange rate regime, and invest more on research and development programs. These objectives would be fulfilled by establishing some international institutions such as World Bank (WB), International Monetary Fund (IMF) and General Agreement on Tariffs and Trade (GATT). Until its collapse, the Bretton Woods system prevailed as the cornerstone of world economic system.

3.2.1.2. Post-Fordist era

The second phase in which finance took more profound effects is labelled as 'the euphoric years' (Dembinski 2009) or 'the era of post-Fordism' (Amin 1994). The apparent feature of this period lies on the shift from Keynesianism (in the central economies) and import substitution industrialisation (in the peripheral economies) towards neoliberalism as a dominant economic policy making (Radice 2005:91).

It is argued that under the neoliberal ideology "human well-being can be best advanced by liberating individual entrepreneurial freedom and skills within an institutional framework characterized by strong property rights, free markets, and free trade" (Harvey 2005:2). As can be inferred, the application of neoliberalist economic policies has paved the way for free movement of capital in the form of goods and services without any boundary lines, which eventually tightens the interdependence of diverse economies and breakdowns economic barriers. Additionally, Kotz (2010:3) explains the economic consequences of neoliberalism as:

> a withdrawal by the state from the role of guiding and regulating economic activity; privatisation of state enterprises and public services; the slashing of state social programs; a shift to regressive forms of taxation; a shift from cooperation between capital and labour to a drive by capital, with aid from the state, to fully dominate labour; and the replacement of co-respective behaviour among large corporations by unrestrained competition. Neoliberalism has an associated ideology of worship of the so-called "free market" along with a denial of any positive role for the state apart from its coercive functions.

In the light of these developments, liberating the market by removing obstacles – trade barriers, the state apparatus, pro-labour policies *etc.* – has transformed the class structure and social formation of societies through which capital owners hold mainly their wealth in the form of financial assets, while the majority of managerial class derives profit in the form of wage/salary and bonuses (Duménil and Lévy 2005).

It is an undoubted fact that the embedding of neoclassical policies in the economic activities ignited rapid economic globalisation and internationalised method of production and distribution. However, the early 1970s unearthed another fact that most of the mature economies were suffering from a significant decline in their economic growth levels and concomitant falling profit rates. As the ramifications of this, advanced economies were now facing a substantial slowdown of capital accumulation, multiplication of inequality gap and more frequent and sharper crisis potential (Lapavitsas 2013:2). Based on these effects, the decline of growth, accumulation crisis and profitability crisis were all associated with the subversive stagnation within the productive sector. It is, hence, important to detect underlying causes of stagnation in the productive sector.

Together with the effect of rising inflation between 1960s and 1970s, one of the rationale for the slowing down of global economy was related to the increasingly competitive environment in the industrialised markets. The competition progressively intensified due to capital owners' pursuit of surplus extraction through technological advancement and new machinery equipment. This, in return, brought over-capacity and additional costs, which eventually result in decrease in investments and profits (Tauss 2012:55). The developments in the labour market, on the other hand, were also significant in the 1960s. In the course of the economic boom, trade unions became more powerful by organising themselves well in the negotiations of labour wage. Subsequently, enforcing employers to compromise on high wage levels, profitability declined further and deepened the crisis (Harvey 2010).

The withering away of economic boom and the crisis of Fordist model of accumulation reached to its peak with the oil shock of 1973 and the collapse of the Bretton Woods system. Beside the oil price shock, as extensively elaborated in the previous section, the end of Bretton Woods system meant that the dollar was no longer convertible to gold and fixed exchange rate regime gave its way to instable exchange and interest rates. Trusting on the neoliberal policies, a new era in the functioning of economic system has been commenced in the wake of the collapse of the Bretton Woods system, known as post-Fordist era. Stagnated production and the profitability crisis had been overcome by mainly deregulating international finance and rising private banking. In other words, the exorbitant profits brought back to capital owners not through boosting production and investment activities in the real sector, but rather through investing on financial markets by some abstract sophistications. Therefore, in general, the expansion of financial sector was a response to the economic downturn (Epstein 2005), and post-Fordism has changed the function of finance from being an ordinary facilitator of accumulation process to be the catalyst behind economic growth (Duménil and Lévy 2005:13).

The new institutional setting is designed by "proliferation of securities markets, risky derivatives trading, massive speculation, the rise of hedge funds" (Tauss 2012:69), "the growth of private financial assets, the rise of financial services, mutual funds and institutional investors" (Deutschmann 2011:377). The money, hence, moved into financial markets to be used in these sectors in order to make abnormal profit. It can also be asserted that the gravity of economic activity shifted into financial sphere, and henceforth "economies are increasingly driven by movements in the price of real estate and financial assets" (Stockhammer 2012:40). At this juncture, the role of information and communication technologies should not be underestimated in terms of their contribution to the expansion of finance (for more details *see*: Dembinski 2009:24).

In the new setting, two revolutionary changes have taken place; 'corporate revolution' and 'managerial revolution'. The former "refers to the formation of large corporations, backed and controlled by finance" (Duménil and Lévy 2001:582). Enjoying largely from the liberalisation of capital movement which necessarily creates international debt relations, these transnational corporations operate within the monopolistic and oligopolistic market structures and stand at the centre of economic activities by aiming at extracting financial profits in lieu of engaging in productive activities that brings relatively lower profits. The shift from production to finance as the main wealth generating mechanism within the corporate revolution necessarily accompanied with rising inequality and social polarisation of income levels. More concretely, inequality and income polarisation worsened by the result of firms' reluctance in investing in productive activities, since profits are often accrued from financial investments, which goes back to financial activity to make more profit. The low levels of productive activities, in return, caused stagnation of real wages; thus, wage earners' indebtedness increased (der Zwan 2014). As the financial sphere seemed shining in the sense of efficiency and profit making, employees in the financial sector received salary much higher than employees in other jobs. Thus, "the rapid distribution of national income towards capital owners and away from labour" (Wade 2005:4), and income generated through financial investment are found to be one of the most important contributors of income inequality and social polarisation (Nau 2013).

Managerial revolution, on the other hand, denotes the transformation of firms, now managed by staffs of managerial and clerical personnel (Chandler Jr 1993). In this new form of management understanding, the gap between workers and their means of production widened, and also the working task being defined by other salaried personnel (Duménil and Lévy 2001:582).

This short survey on the transformation of the role of finance in the last century might seem, at first sight, the synopsis clarifying the transformation of advanced capitalist economies, especially the Anglo-Saxon economies, amongst which the US is predominantly spearheading. However, in fact, developing countries also follow a similar pattern of financialisation logic, albeit it can be conceptualised as 'subordinate financialisation' (Lapavitsas 2013:42). The subordinate character of developing countries' trajectory of financialisation emanates from the project of promoting development in the poor countries. The aim with this project, speciously, seemed to integrate domestic economies into international capital markets under the objective of providing capital flow from rich to poor countries. Nonetheless, the reverse flow of capital took place through the establishment of foreign banks, opening of capital accounts and the accumulation of foreign exchange reserves in the domestic economies. At the end, finance in domestic economies acted as subordinate to the financialisation in the advanced countries (Lapavitsas 2013:43).

The process of subordinating domestic finance to advanced economies is conceptualised by Becker *et al.* (2010) as 'peripheral financialisation'. Accordingly, some peculiarities of financialisation emerged in the peripheral economies as part of the objective of sustaining financialisation in the economies of the centre. Typically, peripheral economies give strong role on interest bearing capital by trusting on banks and keeping interest rates high, rely mostly on capital inflows and targets over-valued currency; however, sustainability of these policies depends upon the existence of over-liquidity in the centre (Becker *et al.* 2010:231). The new international division of labour has also deepened the subordinate character of periphery by concentrating technological development and innovation in the centre, whilst physical production of goods was left to peripheral economies through some control mechanisms located in the centre (Cox 1980:384).

Financialisation, regardless of calling it subordinate, peripheral or hegemonic, is expansive across the globe. As argued by Dore (2002:116–17), its hegemonic power manifests in:

> the increasing dominance of the finance industry in the sum total of economic activity, of financial controllers in the management of corporations, of financial assets among total assets, of marketed securities, and particularly of equities, among financial assets, of the stock market as a market for corporate control in determining corporate strategies, and of fluctuations in the stock market as a determinant of business cycles.

This is also evident in some statistical records. Baker *et al.* (1998:10), for instance, show that the share of funds raised in global financial markets in the overall world exports was 0.5% in 1950, whilst it rose to 20% in 1996. Likewise, the ratio of global financial assets to global GDP rose at least three times (Blankenburg and Palma 2009) in the last three decades. Considering also the growth of debt markets from US$33tn to US$90tn and stock market from US$49tn to US$66tn between 2000 and 2013 (Ro 2014), the control of US corporate equities by money managers (Porter 1992), the rise of the percentage of pension funds in total business equities (Ghilarducci 1992), it can be claimed, without no reservation, that the bulk of the world economic activities are maintained by large-scale expansion and proliferation of financial market operations in the 21st century, which brings finance at the core of economy and wealth generation and changes the entire social formation of contemporary societies, namely centres 'finance'.

3.3. APPROACHES TO FINANCIALISATION: POLITICAL ECONOMY PERSPECTIVES

In this section, various definitions of financialisation are introduced and discussed by also considering the historical rise of finance as elaborated above. In this lens, different approaches towards financialisation is examined through a critical analysis by comparing and contrasting them within a political economy understanding.

In recognition of the fact that intense debates on financialisation phenomenon is yet to burgeon, particularly gained momentum in the wake of the global financial crisis of 2007, a distinct categorisation of the approaches is still possible to construct here to give a comprehensive picture of the existing literature. Prior to this, it should be mentioned, first, that most of the theories on financialisation have somehow benefited from the language of Marxist political economy discourse in rendering the transformative role and gravity of finance in contemporary capitalism. Thus, the influences of Marxist terminology and concepts are explicit in each category. Having said that, approaches towards financialisation can be divided into six categories:

(i) Mainstream approach;
(ii) Marxist political economy approach;
(iii) Post-Keynesian approach;
(iv) Regulationist approach;
(v) Varieties of capitalism approach;
(vi) Cultural economy and heterodox political economy approaches.

The following sections provide brief explanation on each of these approaches to develop a robust understanding of the issues.

3.3.1. Mainstream Approach

The notion of financialisation has not been used by mainstream economists as a specific phenomenon that has detrimental effects on the functioning of economy and society in a broader sense. Instead, they have reflected with positive view upon the remarkable ascent of finance within economic system. Accordingly, it is believed that the proliferation of financial markets would hasten financial development and hence foster economic growth (*see*, amongst others: Ang 2009; Beck *et al.* 2014; Cheng, Ho, and Hou 2014; Levine 1998). Since the declining rates of growth in the 1970s put most economies into economic difficulties, mainstream economists prescribed financial development as the central objective for regeneration of economic boom. Thus, the economic debate has been pursued within such a narrow perspective that confines financialisation to a particular attempt for regaining economic prosperity without taking its social, political and other implications into consideration.

The debates, in particular, seek any causal relationship between financial development and economic growth through large number of empirical studies repeating similar findings in the literature. In line with this, determining robust indicators for financial development and economic growth (Estrada, Park, and Ramayandi 2010; Hachicha and Ben Amar 2015; Hassan, Sanchez, and Yu 2011; Wu, Hou, and Cheng 2010), the role of bank-based or market-based financial systems on economic performance (Chakraborty and Ray 2006; Levine 2002; Uzunkaya 2012), the direction of causality (Christopoulos and Tsionas 2004; Gould, Melecky, and Panterov 2016; Hsueh, Hu, and Tu 2013; Luintel and Khan 1999) and the impact of financial repression or liberalisation (Demetriades and Luintel 2001; Roubini and Sala-i-Martin 1992; Rousseau and Wachtel 2011) have constituted the primary concern associated with the rise of finance.

While the role of finance has been essentialised in the side of mainstream literature, the break out of global financial crisis starting in 2007 disenchanted most economists with regards to their trust in finance-led growth regime. However, a systemic challenge of prevailing neoliberal form of financialisation has never been debated in the mainstream literature. The critical perspective, on the contrary, was addressed mainly by heterodox schools of thought rendered below.

3.3.2. Marxist Political Economy Approach

The early writings on the subject of financialisation, within Marxist perspective, were placed in the socialist journal of *Monthly Review* in the 1970s mainly by Paul Sweezy, Harry Magdoff and Paul Baran. In their approach, financialisation is conceived to be a new form of capital accumulation introduced by rentier class in the presence of systematic stagnation faced within industrial capitalism (Magdoff and Sweezy 1987). Three underlying trends were observed in the new accumulation regime: (i) the slowing down of the rate of growth, (ii) proliferation of monopolistic multinational corporations (MNCs), and (iii) financialisation of the capital accumulation process (Foster 2007:2).

As the substantial slowdown of global economy was evident in the 1970s, as explained in the previous section, MNCs kept generating more surplus that could not be absorbed in the productive sector. In the world that is dominated by monopoly capital, the realisation of surplus has mainly been done through corporations' involvement in bond and equity trading in stock markets. Monopoly capital was, therefore, no longer depended on banks to circulate, for MNCs engage in financial activities on their own accounts (Lapavitsas 2011:620). This should not be construed as the loss of importance in the side of banks; contrarily, banks remained the cornerstone of contemporary finance (Lapavitsas 2013:5). However, they restructured themselves to adapt to the new international economic setting. Accordingly, banks diversified their profits mainly through (i) increasing income shares from client services within service-oriented activities (payment services, expertise, advice, asset management) (Dembinski 2009:46), (ii) borrowing (mortgages, general consumption, education, health), and (iii) expanding financial assets (housing, pensions, insurance, money market funds) (Lapavitsas 2011:620). The overall effect of MNCs and banks, however, led eventually to stagnation in the production sphere, and capital was moved into financial activities to extract surplus principally through speculative ways (Lapavitsas 2011:612).

A more sophisticated approach on financialisation is advanced by Brenner (2004) within the lines of classical Marxism by stressing the impact of over-accumulation and falling profit rates. In this approach, it is argued that the post-war boom accompanied with an expansive over-capacity in the productive sector, which exacerbated competition and lowered profit rates consequently. As a response to the low profitability, the rise of finance was essentialised to generate new exorbitant profits to relieve stagnation (Brenner 2006).

In contrast to the perspective of the *Monthly Review*, which puts 'surplus absorption' at the centre of financialisation debate, Brenner (2004) views the rate of profits to fall and harsh competition amongst the capitalists as the underlying cause of the rise of finance in the 1970s. Meanwhile, Brenner never used the notion of financialisation to address the new accumulation regime based on finance driven industry, whilst others explicitly use it in their analyses.

Having strong affinities with Marxist theory, Arrighi's view on the issue is also of special importance, for he systematically discusses financialisation in the context of his theorisation of 'long cycles of capitalist development', rather than treating it as newly emerged phenomenon or final stage of capitalism (Arrighi 1994). In his long cycles approach, Arrighi (1994) claims that the world capitalist order passed through four cycles since the 13th century as follows: the Genoese cycle between the 15th century and the early 17th century; the Dutch cycle from the late 16th century till the 18th century, the British cycle between the second half of the 18th century and the early 20th century; and the US cycle of the 19th century to the present. Transition from one cycle to the next takes place due to a global crisis of accumulation, which weakens the present hegemonic power and leads to another hegemon coming to power, and hence, starting a new cycle of capitalist development (Arrighi and Silver 1999). One of the most important characteristics of the transition is that financial expansion taking place around the hegemonic power starts to decline and results in crisis. Therefore, in this perspective, financial expansion is not considered as the final stage of capitalism, but rather a repeated pattern at the end of each cycle during the long history of capitalism (Orhangazi 2008:43).

Arrighi's theory is very much reminiscent of Braudel's analysis of capitalism in which financial expansion in the history are treated as 'the sign of autumn' that shows the maturity of certain stage of capitalist development (Braudel 1984). More precisely, Braudel's insight on the recurrent rise of finance corresponds, in Arrighi's understanding, to the financialisation of mature capitalism, which basically functions to protect American hegemony in the world politics, but at the same time signals the autumn of US hegemony (Arrighi 1994).

Critiques to Arrighi mostly address some basic issues such as "the vagueness in the mechanisms of switching to a new hegemonic regime" and "the rationale behind high rates of return in the financial markets comparing to low profits in the real sector due to over-accumulation crisis" (Orhangazi 2008:48), "the uncertainty of identifying new hegemonic regime replacing the current hegemon of [the] US" (Lapavitsas 2013:20), and the ambiguity in identifying the scope of 'wealth redistribution' (Deutschmann 2011:367), which, once cannot be sustained in economic, social and political spheres, leads to termination of financialisation process (Arrighi and Silver 1999:273). Despite Arrighi's theory has some flaws as identified by a number of contenders, it has influenced many studies by bringing the hegemonic power of US at the core of financialisation process of world economies. Gowan (2009), for instance, associates the rise of finance with the dollar being a world money in the control of Wall Street. Similarly, Panitch and Gindin (2009) equates financialisation with the 'Americanisation of finance' that paves the way for universalizing and intensifying the power of US hegemony.

Lastly, and more recently, Lapavitsas (2013, 2011, 2003, 2005, 2012) contributes to the debate on financialisation from his Marxist perspective. In his approach (Lapavitsas 2013:3–4, 2011:611–12) financialisation is

> posited as a systemic transformation of mature capitalist economies that comprises three fundamental elements: first, large non-financial corporations have reduced their reliance on bank loans and have acquired financial capacities; second, banks have expanded their mediating activities in financial markets as well as lending to households; third, households have become increasingly involved in the realm of finance both as debtors and as asset holders.

As can be inferred, Lapavitsas puts much emphasis on the transformation of the functions of economic institutions within the financialisation stream. The financialisation process, in this regard, allows finance capital to dominate economic activity, and generate enormous profits through financial markets regardless of considering the potential outcome of global crisis

(Lapavitsas 2013:1). The extraction of financial profits, in this manner, is provided out of the revenue of workers and other social layers, and hence gives birth to a new set of relations, called 'financial expropriation' (Lapavitsas 2013:39). Financial expropriation does not only confine with exploiting workers, but also entrepreneurs by private asset holders (Deutschmann 2011:382).

3.3.3. Post-Keynesian Approach

Having common ground with some strains of Marxist theory, post-Keynesianism relates financialisation with poor performance in the production sphere that necessarily makes the real sector stationary, while financial sector expands significantly. Similar to, but more substantial than the Marxist view, post-Keynesians put much emphasis on the concept of 'rentier' in identifying financialisation process (*see*: Crotty 1990; Epstein and Jayadev 2005; Pollin 2007 amongst others).

Rentier is defined by Keynes (1936), in his book of *General Theory of Employment, Interest and Money*, as the parasitical entity that derives profits because of exploiting the scarcity-value of capital, and hence lowers the returns of production and investment, and constraints profit making activities for capitalists. The rise of rentier class, thanks to the adoption of neoliberal economic policies, allowed financial profits to become widespread at the expense of industrial profits; hence financialisation induced a substantial slowdown in the real economy (Pollin 2007). The regulation of financial sector is necessary, for this reason, to stimulate productivity, investment, income levels and employment (Crotty and Epstein, 2009).

Crotty (2005), in a more precise expression, argued that the consequences of neoliberal policies posed an important paradox. While, on the one hand, the decrease in global aggregate demand and the intense competition accompanied with low profitability; non-financial corporations (NFCs), on the other hand, became more eager to invest in financial markets wherein real interest rates were raised to make gains in the short-term. Therefore, long-term growth objective adopted by financial markets was superseded by short-termism (Fine 2010:14) for the sake of compensating deleterious effects of competition and slowdown of aggregate demand, which, at the same time, led NFCs to acquire financial assets by using their investment funds, or creating financial subsidiaries (Crotty 2005:34).

The divergence between financial sector and real sector is also addressed, within the post-Keynesian perspective, by Epstein (2005:3) who defines financialisation as "the increasing role of financial motives, financial markets, financial actors and financial institutions in the operation of the domestic and international economies". Based on this definition, it can be claimed that Epstein concentrates only on the scope or extent of financialisation, since he does not specify the impacts of financialisation on society, nor does he give any geography and time period in which it takes place (Sawyer 2013:6). Although lacking precision, this definition still shows pervasive character of financialisation, that might be why it has largely been adopted and cited in the literature.

Epstein's approach towards financialisation is usually compared with Krippner (2005, 2011); yet she is mainly influenced by Arrighi's views rather than favouring post-Keynesian view of financialisation. The comparison is made mostly for delineating the distinction between definitions of financialisation that is limited with the transformation in the last decades and those that can be applicable any time and place without mentioning precision. Krippner (2005:174) favours the first type of definition and states that financialisation is reflected as "the growing weight of finance in the American economy". By essentialising the US economy and its policies in the process of financialisation, she affirms the Arrighian view of the long cycles of capitalist development. She also presents alternative definition of financialisation, but this time more evocative of Braudel's perspective, "as a pattern of accumulation in which profits accrue primarily through financial channels rather than through trade and commodity production" (Krippner 2005:174). As such, non-financial firms rely more on financial investments to derive revenues therein in spite of applying traditional productive activities (Krippner 2011:34). What makes Krippner's approach distinct is her success of providing a ground for theoretical claims of Arrighi, *Monthly Review* and others by empirically evidencing the growing weight of financial profits both for financial and non-financial sector within the economy (Lapavitsas 2013:20).

Along with Krippner, Stockhammer (2004) also provides empirical support to the financialisation of NFCs investment. Adopting a post-Keynesian view on financialisation, he primarily sees financial deregulation and polarisation of income distribution as the root causes of economic crisis (Stockhammer 2012). Along this line, his empirical analysis shows how a rise in investment in financial assets gives rise to slowdown of the accumulation of physical assets, at the end of which NFCs become more rentier-like (Stockhammer 2004:719).

As last remarks on post-Keynesian view of financialisation, Orhangazi (2008:6) should be mentioned, who invariably considers financialisation as the proliferation of the size and significance of financial markets and institutions, with particularly stress on the changing relationship between NFCs and financial markets. Drawing a sequential pattern of financialisation, he starts with an accumulation crisis in the 1970s, which subsequently welcomed financial market liberalisation and deregulation. Accordingly, the crisis has worsened corporate performance and NFCs' profitability, which eventually enforced them to increase their investment on financial markets. Resultantly, long-term growth strategies were replaced by short-term oriented financial investments, and finance prominently centred at the core of economic activities (Orhangazi 2008:74).

The post-Keynesian approach, elaborated above, deals with the performative aspects of real economy reshaped after the significant rise of financial markets. In doing so, the debate is pursued mainly around the motivation behind generating financial profits by NFCs in the short-term, while long-run investment projects are abandoned in the real sector that culminated in slowdown of economy.

3.3.4. Regulationist Approach

Originally emerged from the Marxist tradition, and later referring to the post-Keynesian and institutionalist theories, regulationist approach basically addresses the ways to stabilise tensions of capitalist economy that periodically bring about inherent crisis and contradictions.[25] In responding to this, regulationist approach suggests some sets of regulatory structural forms such as wage relations, monetary and ecological restrictions (Jessop and Sum 2006). However, regulation is considered, here, to be much broader concept than state intervention or technical understanding of regulation and encompasses social norms as well (Becker *et al.* 2010:226).

The regulationist view of financialisation proclaims the end of Fordist era in the 1970s, which at the same time harbingers a new regime of accumulation based on financial dominance. The characteristics of the Fordist regime were mass production, increased wages and productivity, whilst post-Fordist regime is commemorated with the ascendance of finance as a particular regime of accumulation. Boyer (2000) adopts the concept of 'finance-led growth' to describe the new regime of accumulation wherein Fordist capital-labour compromise collapsed and gave way to decentralisation and individualisation of labour wages and contracts. In addition, previous forms of oligopolistic competition broke down in the aftermath of financial liberalisation policies that allowed opening of domestic markets to foreign competition. A subsequent change in wage-labour nexus, eventually, ended up with favouring the interests of

[25] The most recent and severely devastating crisis are (i) the oil crisis in 1974-1975, (ii) the debt crisis in the peripheral countries in 1982, (iii) the U.S. stock market crash in 1987, (iv) the savings and loan crisis between 1985 and 1990, (v) the Asian financial crisis in 1997, (vi) the 'millennium economy' crash in 2000, and (vii) the global financial crisis in 2007 (*see*: Altvater 2009; Toporowski 2005).

creditors and shareholders. The new economy based on high technology and the intensification of service industry for consumers is now governed and encompassed by the power of shareholders, which, in return, reduces market share and profitability (Boyer 2000:143).

Boyer's finance-led growth model, though providing an authentic view of financialisation, has been subject to some criticisms. For instance, it is expressed that Boyer's model is set "in the context of a closed economy and do not contain a theory of firms' financial policies and financial asset price determination" (Van Treeck 2009:919). More substantially, Becker *et al.* (2010) and Becker and Jager (2010) argue that Boyer (2000) proposes an abstract model of finance-led growth regime that approaches accumulation process one-dimensionally. This, hence, makes the new growth regime is only applicable to the US and the UK economies as claimed by Boyer (2013). However, Becker and Jaeger (2010) provide a multidimensional approach to accumulation process by which the impact of financialisation in the peripheral economies is acknowledged. Accordingly, they suggest three typological axes of financialisation: first, productive/financialised accumulation; second, extensive/intensive accumulation; third, introverted/extroverted accumulation (Becker and Jäger 2010). Explaining not only the financialisation process of central but also that of peripheral economies, four types of financialisation are postulated based on (Lapavitsas 2013:23): (i) based on 'fictitious' capital, by which is meant inflation of financial prices; (ii) based on interest-bearing capital, meaning expansion of banks; (iii) 'elite', implying the involvement of the bourgeoisie and the upper middle class; (iv) 'popular', indicating that workers have also been drawn into financial operations".

Regulations view concentrates more on the political economy roots of financialisation that are characterised by accumulation crisis. Not substantively different from the previous approaches but more on the policy level, this approach suggests regulatory adjustments upon the prevailing financial structure to avert the implications of accumulation crisis.

3.3.5. Varieties of Capitalism Approach

As can be inferred from the notion of 'varieties of capitalism', this approach evaluates financialisation in the context of changing characteristics of capitalism in its various phases. Similar to others, the approach has broad affinities with the Marxist and regulationist perspectives on financialisation. Accordingly, the shift in the last century, from Fordist to post-Fordist regime of accumulation, is hypothesized as transition from productionism to 'coupon pool' or financialised capitalism under the varieties of capitalism view (Froud *et al.* 2000, 2001, 2006; Froud, Leaver, and Williams 2007). While capital markets simply have an intermediation role between household savings and investing firms in the productionist form of capitalism, coupon pool capitalism, contrarily, structures capital markets to regulate both household and firm behaviour. In doing so, the regulatory role is given to 'coupons', which are known as "different kinds of financial paper (bonds and shares) traded in the capital markets" (Froud, Johal, and Williams 2002:126).

The significance of changing role of capital markets from intermediation to regulation shines out with the rise of shareholder value maximisation, which is induced by a fundamental change in corporate strategy. In this vein, the change was triggered with NFCs' renouncement from 'retain and reinvest strategy' that aims at long-term profitability towards 'downsize and distribute strategy' wherein corporate labour force was downsized, and a higher share of earnings were distributed to shareholders (Lazonick and O'sullivan 2000). This process commenced initially with declining corporate profits, low stock prices and increased power of institutional investors and mutual funds in the 1970s, and later accompanied with increased shareholder pressure on management through forcing managers to give more response towards shareholder value maximisation (Useem 1993). Beyond their usual role of skilled professionals, managers were now coerced to act as agents of shareholder interests.

Shareholder value orientation eventually ended up with the loss of social basis of prosperity, albeit the efficient market hypothesis contrarily claims that social welfare is maximized when all firms in an economy maximize total firm value (Davis and Kim 2015:209–10). It has also caused the fade away of economic dynamism due to short-term decisions of financial markets (Orhangazi 2008:63).

Beside the corporate dimension, financialised capitalism also shows its distinctiveness through "massification of household savings …, a dramatic growth in the group of financial intermediaries and feedback effects on the calculations of firms and households" (Erturk 2008:26). As a result of strengthening of finance through continuous appreciation of financial assets such as pensions, mutual funds, share portfolios and *etc.* (Aalbers 2008), corporations are subject to ongoing effects of financial market pressures in the new economic structuring (Feng *et al.* 2001).

The most detrimental effect of coupon pool capitalism, within the perspective of the varieties of capitalism, is that the economy is much vulnerable to economic turmoil and unable to generate long-term financial security in the financialised regime (Erturk 2008:29).

3.3.6. Cultural Economy and Heterodox Political Economy Approaches

While economy wide macro implications of financialisation were addressed in the previous five approaches, cultural economists primarily seek the influences of finance-dominated economic structuring on some spheres of everyday life (*see*: Aitken 2007; Dore 2000; Fine 2010; French and Kneale 2009; Haiven 2014; Jameson 1997; Langley 2008; Leyshon and Thrift 2007; Martin 2002 amongst otheres). In this lens, financialisation is defined as a phenomenon that culminates in everyday life practices of people encompassed by and subordinated to the objectives of financial world (Martin 2002). Accordingly, "the home is increasingly seen as a real estate investment, personal relationships get infused with monetary concerns and decisions are taken with an eye on their credit rating implications" (Pellandini-Simányi, Hammer, and Vargha 2015:734). In the individual scale, traditional hard work ethic withered away under the influences of market populism and new cultural ideology of hedonistic and post-materialistic value orientations, which raised the aspirations of immediate way to acquire unlimited financial wealth (Deutschmann 2011:362). Everything around us, therefore, is redefined with financial terminology and filtered with some cost-benefit analysis and portfolio selection that necessarily accompanies a financialised worldview permeating through every sphere of individual life and creating financial identities.

The creation of financial identities is, in particular, of special importance since it is closely associated with the process of financial subject formation in the neoliberal era. Specifically, financial identities are idealised in the 1980s under the neoliberal discourse of personal responsibility and efficiency within the financial area to create everyday investors appearing as "artifacts of, not architects in, processes of change" (Langley 2007:73). The embedding of investor practices in everyday life is also reflected by Harmes (2001) with the influence of Gramscian accounts of power. Harmes (2001:103) points the importance of making investor identities and the emergence of a broad investment culture that strengthens the hegemonic power of finance capital.

The existing literature is abundant in some studies on everyday life financialisation. These include the social meaning of money (Zelizer 1997), cultural economy of finance (Pryke and Du Gay 2007), the contribution of life assurance to the financialisation of everyday life (French and Kneale 2009), Walmart's role on financialisation through a cultural idiom of securitisation (Haiven 2014), coffee industry and financialisation (Newman 2009), financialisation of micro-credit (Aitken 2013), and financialisation of water (Bayliss 2014). Specially focusing on the case of housing, in the modern period, households no longer consider houses primarily to function as homes to shelter and live with family members, but they rather see acquiring houses as an investment, “something to put equity into and take equity from” (Aalbers 2008:152). Investment, in return, necessarily brings about risk; however, this time risk is borne in the realm of everyday practice.

The rationale behind households’ excessive involvement in financial activities is addressed by Martin (2002) who emphasises the retreat of Keynesian state and its social support system, which transferred its functional role to private initiative. Similarly, Dore (2000) argues that the market economy paradigm operating under the notion of invisible hand withdraws state and its social support system from the public realm and lets individuals alone with overcoming their economic problems in disguise of free entrepreneurship. This, hence, forces households to invoke financial institutions against their economic troubles. While Martin (2002) and Dore (2000) adopt a Keynesian state perspective in obviating household financialisation, it is important to note that despite rendering an essential role to it, state should be seen as the facilitator of financialisation in the modern period. It should be, for this reason, recognised that modern nation states are not victims of financialisation process in a sense of losing their exertive power over economic institutions; contrarily, financialisation depends on states by their active and continuous intervention on the economy such as regulating financial system and capital adequacy, managing risks and rules of competition among financial institutions, intervention to underwrite the solvency of banks, and providing enough liquidity and *etc*. (Lapavitsas 2013:3).

Notwithstanding their essential role in designing the structure of domestic economy in the interests of financial ascendance, the traditional function of states has weakened and transformed in the international scope due mainly to financial globalisation, which paved the way for establishing supranational states with their own rules, actions and influence areas. In this new international setting or the global order, states are becoming societies with no power base; instead, international institutions –such as World Bank, IMF, OECD and WTO- lead the world economic system through financial markets and mammoth business undertakings (Ramonet 1997). The old state apparatus, hence, remains under the pressure of financial institutions. As an articulation of this, investors gain profit from rising interest payments on state bonds, investors’ capital never remains idle due to their pressure on governments to open new outlets, and states act as private financial corporations operating in the financial markets (Deutschmann 2011:361).

Financialisation has also been debated under some heterodox political economy perspectives. In delineating its significance, Dembinski (2009:6) argues that "financial thinking has gradually permeated and transformed behaviour patterns, mechanisms and structures, and extended its control over society to the point where it is now one of its main organizing principles, or indeed the dominant one". This process is referred, in his words, as 'financialisation' through which economy and society – primarily in the Western world –are reorganised around the search for financial efficiency.

In its state of art, finance, as the main organizing principle, replaced the network of relationships in the society with a stunning display of transactions[26] (Dembinski 2009:138). The evaporation of relationships within the society, therefore, culminated in the construction of 'portfolio society' in which "the investment idiom becomes a dominant way of understanding the individual's place in society" (Davis 2009:6). The notion of 'common good' (Bovée 2008) loses its basic function in the portfolio society from being 'each individual's contribution to the solidarity and harmony of society' and turns out to be some compensatory and regulatory changes initiated by governments in the name of 'public good'. Once the common good is taken from the sphere of civil society and made subservient to the aspirations of financial world, "the market, like the rest of society, became a battlefield where all the players are out to maximize immediate efficiency – remuneration as spoils of war – and then swiftly transfer it to the private sphere in order to build a fortress of lonely individual happiness" (Dembinski 2009:65).

The altering effect of finance on existing relationships within the society is, likewise, addressed by Fimbel *et al.* (2015:76) through essentialising the notion of 'demateriality', which he defines "as a substratum creating new conditions for relationships within the social fabric". In this regard, while initially currency, credit and securities were dematerialised; subsequently, traditional relationships based mainly on proximity and loyalty had been broken up for the sake of forming new economic relationships between producers, consumers and suppliers. Consequently, not only society has been embedded within the economy; but economy has also been embedded within finance, which together signify 'double embedding' (Fimbel *et al.* 2015:78). The process of double embedding, however, is identified, in Fimbel *et al.'s* (2015) understanding with 'marketisation' that establishes structuring role of demateriality. Since the process of embeddedness is signified by economy and finance, this constitutes dis-

[26] The shift from relationships to transactions is discussed in the next section by also emphasizing the role of trust in the new transaction society.

embeddedness in Polanyian discourse, which is an important consequence of financialisation within political economy context.

In reflecting the approaches to financialisation discussed above, they all propound certain explanations for the remarkable rise of finance in the gravity of economic activities. It is obvious that the main focus with the first five approaches is primarily towards exploring macroeconomic effects of financialisation within the economy by stressing particularly on the changing roles and flourishing of new financial institutions, and the emergence of new financial ways of profit making. The wider societal consequences of financialisation and its effect on individual behavioural pattern and cultural aura, however, have been given limited attention throughout the debates. Cultural economy and some heterodox political economy approaches to financialisation, though very limited, fill such an important gap in the literature.

Following sections render a critical perspective on the financialisation theories elaborated under six different approaches above. In doing so, it develops a moral economy understanding to crystallise the nature and dimensions of financialisation. However, before doing this, recent empirical studies on financialisation is surveyed in the next subsection to elaborate on to what extent theoretical dimensions of financialisation throughout six categories has been empirically examined. This gives us some particular evaluation techniques of financialised economies in an econometric analysis.

3.3.7. Review of Recent Empirical Studies on Financialisation

While the theoretical literature on financialisation is considerably limited but comprehensively dealt with, empirical studies mostly concentrate on certain dimensions and implications of financialisation on economy and society. In this lens, widely used indicators of financialisation in the existing literature is rendered in the Table 3.1. As financialisation phenomenon is associated with the rise of financial sector against the decline in the real sector performance, some studies empirically examine this relationship by using country-level and firm level data. Demir (2009), for instance, analyses real investment performance of firms in three emerging markets in the existence of rate of return gap in financial and fixed investment areas. Therefore, the study finds that short-term financial sector investment alternative is chosen by most of firms, which, in return, reduces the real economy performance. Similar to Demir (2009), Orhangazi (2008) explores the firm level interest upon real investment areas in the US economy. The empirical examination consisting of a sample of non-financial corporations between 1973 and 2003 reveals an adverse relationship between US financialisation and real investment, due to mainly the expansion and profitability of financial investment areas, which in return, changes the incentive mechanism of firm managers to invest more on financial sector. Another firm-level panel data analysis on financialisation is conducted by Tori and Onaran (2015) on the UK economy. Accordingly, empirical evidence suggests that the selected non-financial corporations are less likely to engage in physical investment due to the high rates of return in financial sector investment so that productivity and growth in economy replaces with stagnation and fragility.

Financialisation is also linked in the relevant empirical literature to the socioeconomic parameters. Amongst them, distributional issues such as income inequality and share of employment in the financial sector have been mostly preferred indicators of financialisation. Using panel data analysis for the OECD countries, Assa (2012) analyses the impact of financialisation on inequality, unemployment and growth. The empirical evidence strongly suggests that the financialisation trend negatively effects these three variables by causing slow growth rates of GDP, exacerbating employment opportunities and increasing economic inequality. Another study on OECD countries and their positioning against financialisation trend is addressed by Dünhaupt (2014), who assumes that the changing corporate governance understanding with neoliberal policies brought about shareholder value orientation, which, in return, increased income inequality. The results suggest that the top income shares are positively affected from stock market capitalisation and dividend payments. Golebiowski *et al.* (2017), similarly, examines the relationship between financialisation and income inequality, and find that income inequality and unemployment factors are widely determined by the orientation towards financialisation. Hyde *et al.* (2018) deals with inequality issue in most developed capitalist societies. By dividing inequality into three categories as market-generated, state-mediated and distributional inequality, Hyde *et al.* (2018) found that financialisation in the form of (i) finance, insurance, and real estate employment; (ii) credit expansion; and (iii) financial crises all negatively affect three categories of inequality.

Apart from the approaches above, financialisation is also considered in the developments of the rise of financial sector variables. Particularly focusing on emerging markets rather than taking advantage of widely disclosed data of firms in advanced countries such as the US and the UK, Karwowski and Stockhammer (2017) compares the degree of financialisation in advanced and emerging market by looking at some indicators including stock market influence, capital inflows, private sector and household debt. The study concludes that financialisation is more pervasive in the advanced countries than that in emerging economies. Raza *et al.* (2015) reckons with financial depth, credit growth and deposit liabilities of the financial sector as the indicators of financialisation. Their results indicate that the trade openness deepens financialisation in the observed countries due to the fact that it increases foreign rentiers' profit. In examining financialisation in the case of an emerging economy, Tellalbasi and Kaya (2013) empirically examines the financialisation of companies listed in the Istanbul Stock Exchange's Industrial Index. By dissecting financial payments, debts and profits of these companies, they conclude that financial benefits have an adverse effect on the number of real investment activities.

Financialisation is associated, alternatively, with the size of financial profits generated by firms and other institutions. Alexiou and Nellis (2016) sheds light on the motivations behind investing on industrial profits and financial profits. They conclude that the investment decisions under the temptation of capital accumulation pave the way for opting for financial profits, which in most of the case, provide higher returns than industrial profits. In a similar line, Krippner (2005) investigates the financialisation trend in the US economy in the post-1970 period in his seminal work. It is suggested that the rise of finance shapes accumulation patterns; thereby, the role of state on investment areas has been totally changed in the face of globalisation together with the rise of new economic powers of modern corporations.

The relationship between financialisation and economic growth is also examined in the relevant literature quite recently. Assuming that non-financial corporations should trigger more economic performance than financial corporations, Tomaskovic-Devey *et al.* (2015) argue and evidence that the financial investments of non-financial corporations lead to stagnation in economic growth due to the decline of value-added caused by financialisation.

The short survey on the literature of financialisation invariably evidences that the financialisation phenomenon has destructive effects on social and economic life, particularly on distributional issues and macroeconomic dimensions. Since the empirical investigation of everyday life in the presence of financialisation has not been dealt yet, the literature can be expanded by locating this aspect into the analysis.

Table 3.1: Widely Used Measures of Financialisation

Studies	Indicators of Financialisation
Alexiou and Nellis (2016)	Industry's value added as % of GDP Manufacturing value added as % of GDP Employment in industry (% of total employment)
Assa (2012)	Value added in finance as a percentage of total value added Employment in finance as a percentage of total employment
Tomaskovic-Devey *et al.* (2015)	Financial assets divided by total assets
Dünhaupt (2014)	Stock market capitalisation, i.e. the value of listed shares as a share of GDP. Net dividend payments of nonfinancial corporations related to their value added
Freeman (2010)	Financial sector's share of profits, The ratio of financial-sector profits to the wages and salaries of all private-sector workers, The ratio of financial assets divided by GDP
Golebiowski *et al.* (2017)	The contribution of the financial sector (FIRE) to total value added The proportion of the employed in the FIRE sector in the total employment Private debt to GDP ratio
Haruna (2012)	Stock market capitalisation to GDP ratio Turnover ratio (valued trade/market capitalisation) Value traded ratio (value traded/GDP)
Hyde *et al.* (2018)	FIRE employment (finance, insurance and real estate) measured as the percent of the labor force employed in FIRE industries Credit expansion measured as the stock of domestic credit provided by financial institutions to the private sector as a percent of GDP.
Kedrosky and Stangler (2011)	The size of the financial sector as a percentage of GDP
Krippner (2005)	Portfolio income of non-financial firms Profits of financial vs. non-financial firms
Kus (2012)	Financialisation index created by averaging the standardized scores of three major indicators (bank profitability, value of total stock traded, and securities under bank assets)
Raza *et al.* (2015)	Stock of liquid liabilities, M3 to GDP Private credit to GDP Deposit liabilities of the financial sector
Stockhammer (2004)	Interest and dividend income ('rentiers' income') of non-financial businesses

3.4. MORAL ECONOMY UNDERSTANDING BEYOND MARXIST DISCOURSE: A CRITICAL PERSPECTIVE ON THE LITERATURE

The literature, surveyed in the preceding section, embraces different perspectives on the rise of modern finance in the gravity of economic activities, and its implications on economy, society, politics, culture and so on. Despite the fact that political economy aspects of financialisation have been addressed throughout the literature by also referring to the transformational role of finance as an ordinary practice of everyday life into an exclusive realm within the economy, the emphasis on the nature and detrimental effects of financialisation remain limited with the positivist and materialistic class-based understanding of Marxist political economy. In line with this, even alternative perspectives on the notion of financialisation have broad affinities with Marxist theory and its terminology that essentialises such concepts of accumulation crisis, surplus absorption, monopoly finance capital, rentier and so on. The single-perspective based approach on financialisation, hence, precludes the flourishing of alternative perspectives beyond Marxist paradigm.

This study argues that financialisation is a broad concept that must be approached within political economy framework that does not necessarily bound with Marxist theory. Along this, it suggests an Islamic political economy approach to finance and hence financialisation through which the nature, evolvement and burdens of financialised economies together with its implications on individual and social life are reconsidered in the light of Islamic ontology and epistemology. The following two sections, accordingly, deploy a critical discourse analysis on financialisation within Islamic political economy perspective by giving particular attention to the exploration of financialisation of Islamic finance. In doing so, Polanyian understanding of embeddedness is adopted to address how financialisation within Islamic finance impacts social formation of Muslim societies by creating commodification and disembedment through Islamic finance operations.

In order to provide a historical and theoretical base for the objectives above, first, the distinction between market economy and moral economy, and the Polanyian view of double movement – the interaction between economy and society- is elaborated. Later, the definition, scope and characteristics of Islamic moral economy is discussed by giving particular importance to the paradigmatic distinction from others, which necessarily criticizes the mainstream functioning of finance and Islamic finance both, since the common logic behind these two takes their nourishments from the neoclassical economic paradigm.

3.4.1. Morality and Economy

It should be kept in mind that the interaction between morality and other institutionalised settings of society –law, politics, religion, state and *etc.* – has continuous, transformative and transitive nature such that all the settings are intermingled and support each other, which in turn, lead us to ponder the notion of morality from a multifaceted perspective. When the interaction between morality and economy is considered from this perspective (*see*: Cowley 2005; Hardin 1992; Sen 1990; Zamir and Medina 2010), it is evident, especially in the pre-capitalist societies, that the productive and distributional objectives of the economic structure were derived from the values, norms, rights and responsibilities of a society. In other words, the functioning of economy was subordinated to the pursuit of a good life and societal beneficence, which corresponds to the two vital conceptions, *falah* and *ihsan*, in the Islamic moral economy literature that are discussed later. In this manner, it can be acknowledged that the pre-capitalist societies had portrayed moral economies in which moral norms played a constitutive role over the economic framework and hence economic activities and relations were not left to the determinacy of economic factors. Finance, in the same vein, was driven by the whole objective of establishing social welfare beyond its current role of dominating the entire economy with the purpose of changing social formation and creating financial identities.

In the modern period, the advent of capitalism in concomitance with the Enlightenment process envisaged the notion of economics as an independent and self-proclaimed science, which has challenged the idea of moral economy (*see*: Palmer 2011) such that economics first digressed itself from the political economic outlook and later declared its autonomy and atomisation by breaking its bonds from social formation of society through claiming to be a value-free and self-regulating system. This gave rise to the critique of capitalist system of economics from the perspective of moral economy.

3.4.2. Moral Economy, Market Economy and the Problem of Embeddedness

Moral economy debates mainly concentrate its approach and critique towards the prevailing modern economic theorising on two aspects: the former essentialises conceptual distinction of moral economy from economics, and the latter examines the social formational outcomes or the consequentialist dimension concomitant with this conceptualisation, that is the aspirational embedded society against self-regulating, atomized or autonomous society (*see*: Götz 2015).

To elaborate on the concept first, it can be stated that moral economy comprises a set of relationships, beliefs and norms that together constitute a certain way of socioeconomic life. It embraces a particular kind of economy in which values and norms of society are embedded in the existing institutional structure, and social relations and behavioural patterns are not moulded or determined by merely economic factors, for moral norms play a constitutive role over the functioning of economy through non-economic factors (Etzioni 1988; Sayer 2007). In this respect, moral economists claim that market economy has 'corrupting effects on society' (O'neill 1998), since it dehumanises economic relations into mechanical operations by neglecting societal consequences of these relations through relegating the valuing of things, relationships and ways of life to only economic level.

Moral economy debates in the 20th century have come into the fore with two distinct approaches, one of which essentialises moral economy to evaluate systemic and functional dimensions of exchange mechanisms (Booth 1994; Polanyi 1944), and the latter uses moral economy to evaluate the causes for rebellious and insurgent behavioural patterns of societies (Arnold 2001; Scott 1976; Thompson 1971). It is evident that the majority of the debates on moral economy are primarily indebted to Polanyi (1944), who with his seminal work of *Great Transformation*, has widen the horizons of political economists, sociologists and anthropologists.

Polanyi centres his substantivist approach under the master concept of 'embeddedness' (for further reading on Polanyi and his concept of embeddedness, *see*: Block 2003; Gemici 2008; Hejeebu and McCloskey 1999). In this regard, he critiques market economy due to its disembedded nature which ignores noneconomic forms, such as values, moral norms, kinship, political and religious institutions to be the driving forces over the functioning of economic structure. In Polanyi's ideal world of embedded society, human interchange, and economic life in particular, is submerged in social relations and society naturally envelops its institutions, including economy. The embedded economy, according to Polanyi (1944), hence, existed since archaic times until the emergence of premarket societies. However, in the disembedded economies, self-regulating and pervasive character of economy autonomously functions and carries its operations without subordinating its *raison d'etre* to establish a good life by accepting no superior factor to rule; hence, contrary to expectations, it envelops entire society through making social relations an epiphenomenon of market and exerts its iron rules externally over non-economic institutions and social relationships. The tendency of disembedding economy, by definition, has resulted in a totally different form of social formation, which necessarily leads to the malaise of society by creating fictitious commodities through commoditisation. The objective, according to Polanyi, must be to re-embed economy in society by rescuing land, labour and money from the overarching stream of commoditisation and unregulated market forces or system.

It should be noted that Polanyi never admits the existence of a fully disembedded and fully self-regulated economy to be successful hitherto, as he calls it "a stark Utopia" (Polanyi 1944:3). Instead, he underscores that the classical economists aspired to create an autonomous society wherein economy is effectively disembedded. This objective was imposed on politicians to fulfil; however, it was impossible to achieve this goal. Otherwise, the fully disembedded economy would necessarily accompany with turning out everything to be fictitious commodities, which would destroy human beings and his surroundings into wilderness (Polanyi 1944:3). Polanyi (1944:136) identifies this view with his powerful argument of 'double movement' defined as:

> The social history of our time is the result of a double movement: The one is the principle of economic liberalism, aiming at the establishment of a self- regulating market; the other is the principle of social protection, aiming at the conservation of man and nature as productive organisation.

With this double-movement term, Polanyi (1944) argues that there are two opposing movements in the market societies: the *laissez-faire* movement and the protective counter-movement. While the former endeavours to engrave market understanding to the codes of society through disembedding economy from society, the latter resists the idea of disembedding by developing protective ways to rebalance the degree of embeddedness. The protectivist countermovement, contrary to the Marxist understanding, does not only compose of working class, but rather includes all layers of society. As can be inferred, the continuous conflict between these two movements settle a certain degree of embeddedness in the entire spectrum of various stability levels. Polanyi's thesis of double movement is notable in the sense that there are no longer two strict choices of economic systems as market capitalism and socialism once looked from the perspective of embeddedness, for markets can be embedded in different degrees, which, in return, construes various possibilities beyond these two systems.

Beside his repeatedly mentioning of the 'utopia', a closer and critical insight on Polanyi should be introduced here, though going deeper is beyond the scope of this study. Accordingly, Granovetter (1985) claims that the level embeddedness of economic behaviour in nonmarket forms of societies was lower than what substantivists - primarily Polanyi - claim, as modern period has changed this level less as contrary to the claims. Nevertheless, he suggests that this level is more substantial than those of formalists' views. In this line, Granovetter emphasises the two extremes of undersocialised and oversocialised conceptions of human action where the former is adopted by utilitarian and Hobbesian view to claim that there is no relational and structural social factor that has determinant role on production, distribution and consumption (modes of production). The latter approach of oversocialised human action is used mostly by sociologists and rests on the idea that individual behaviour is an outcome of the social relations in the society in which they always engage. Therefore, customs, norms and habits are followed mechanically, recognizing individual choice mostly shaped by these factors. Granovetter (1985) rejects both extremes and claims that, beyond adopting an atomized human action in undersocialised and oversocialised conceptions, human behaviour is embedded in networks of interpersonal relations (Granovetter 1985:504).

A more fundamental critique to Polanyi was directed by Sayer (2007) by arguing that treating constitutive moral norms as forms of embedding necessarily abstracts its moral content, thereby it de-naturalises social relationships and leads to subjectivisation of values, which, in return, produces soft accounts of capitalism, albeit Polanyi claims the *vice versa*. Lastly, Booth (1994) composes some evidences to critically approach Polanyi such as the evidence of economising behaviour in nonmarket context in classical Greece, or seemingly nonmarket forms to be 'marketlike' (firms, families and governments). Booth (1994:661), then, concludes that "there was indeed a great transformation, but it might be better expressed as a move from a community and its economy (heavily encroached upon by hierarchy and status) to a society in which a certain equality and autonomy were accorded primacy".

Another distinct approach focuses on observational studies on the causes for rebellious and insurgent behavioural patterns of certain societies to associate these causes with jeopardising moral economy nature and social consensus in that society. Thompson (1971), with his seminal work *The Moral Economy of the English Crowd in the Eighteenth Century* examples the food riots of the early 18th century in Britain which were triggered off by such grievances of high food prices, unemployment, malpractices of dealers and a devastating dearth at the end. Since the social environment and the life of Trobriand Islanders, the rioters therein, were regulated by social norms and reciprocities beyond market exchange, these grievances were displeased under the umbrella of consensus through which legitimate and illegitimate behaviour in every sphere of life including market, politics and culture is identified. Thus, social norms and obligations constitute the moral economy of the poor (Thompson 1971).

In proposing a comprehensive rationale for the riot behaviour, Thompson (1971) argues that the transition from moral economy to modern self-regulating market society accompanied with adopting cash-nexus in lieu of bread-nexus; hence, it caused a shift in social formation which was immediately rejected by existing consensus and communal legitimacy understanding of embedded society. Therefore, riot behaviour was seen the remedy to circumvent the impositions of new social formation.

With a similar approach, Scott (1976) analyses the peasant rebellions and their village economy structure in the twentieth century Burma and Vietnam. His main focus is to explain how the village economy is organized around the whole objective of securing peasants' subsistence rights and needs, and how rebellious practices in these villages took place as a result of nonfulfillment of this objective. By doing so, Scott (1976) first argues that the village economy is subservient to or embedded in a moral universe which enshrines the establishment of justice amongst society, through securing subsistence rights for all society members, and the setting of just price. Hence, it becomes a moral expectation for peasant villagers to pursue their subsistence rights through a continuous redistribution process within the society. This approach is in great contrast with the materialistic welfare understanding which construes, from the entire story of village economy, a risk minimisation objective through securing subsistence rights and economising practice behind the rationale for peasant behaviour (Booth 1994:654).

As observed in Thompson's approach, Scott likewise constructs his discourse of moral economy from the perspective of conflict and resistance. In this lens, rebellious behaviours of peasants, according to Scott (1976), should mainly be regarded as the reflection of their insistence on rejecting the European colonialist circumscription which aims to extinguish the ancient ways of peasant life in order to restore a new social formation that allows for the maximisation of European interests at the expense of peasant rights. Therefore, the entire struggle is to preserve the "shared moral universe of peasants" (Scott 1976:167) from the toxic nature of market economy, which is sanctified to actualise European interests by trifling away the subsistence rights through letting the price mechanism and market exchange to rule and decide on it. The village economy, as part of shared moral universe, would, hence, embed its use of land, redistributive patterns and reciprocity into noneconomic norms and institutions.

As Scott claims embedded moral behaviour of peasants in the village economy against pure materialistic and individualistic readings of it, critiques come mostly from this tension by arguing that the village economy still holds the economizing practice – through risk insurance, preserving from hunger and recognizing scarcity of means – so that economic reasoning is there and the functioning of the village economy can easily be evaluated from an economic analysis (Booth 1994:659). Also, the Granovetterian notions of undersocialisation and oversocialisation are widespread to use as a critique to Scott's views. In addition, and beyond these particular issues, it is also subject to criticism that such political scientists can hardly explain “the non-rebellious moral economies of market structured communities” (Arnold 2001:89).

As the discussion so far identifies, moral economy does not provide a particular deterministic role to ‘finance’ beyond being a source of intermediation, as the creation of value and the determinacy of surplus value is assumed to take place within the embedded nature of the economy. Hence, non-economic and non-financial forces, namely values and norms of society play a deterministic role in value creation and in the distribution of surplus value. In other words, in the modes of production purported by moral economy, finance is not considered as the source of value creation, unlike the financialised market economy in which finance is central to all economic system in determining surplus value. The next section, hence, takes the debate into a step further into Islamic moral economy, which aims to de-centre finance more.

3.5. THE BOURGEONING OF ISLAMIC MORAL ECONOMY: A SHORT HISTORY

Whilst the significant rise of capitalism was met by a counterhegemonic discourse by the Western academics in the 18th century Europe, which later opened up the literature on moral economy and its use as a strong critique to capitalist economic system, Muslim scholarship, on the other hand, responded to capitalist penetration in a different manner such that the debates on Islamic economic morality, which should be considered to be a subfield under the rubric of general theme of moral economy, and its articulation on modern economic institutions remained peripheral.

As the Muslim societies were facing many challenges in the post-colonial period, including international political power decline, prevalence of nationalist movements, an ever-increasing stream of liberal and secular worldviews and the effect of globalisation, they strived either for adopting capitalist mode of production through imposition to establish a particular social formation that is alien to its society (for example Kemalist revolution and the establishment of Turkish Republic), or they searched for an authentic Muslim identity that avoids interacting with Western secular worldview and enables Muslims to construct their own social formation through the Islamic worldview in the modern era. Although it was expected that the overcoming challenges and the aspirations of establishing authentic Muslim identity would bring the issue of Islamic morality into the centre of academic debate, it rather worked the other way around and culminated in a hybrid and malaise understanding of economic system which ruled out the flourishing of IME in the Muslim thought. The consequences of hybridity and mimicry has given birth to the theory of Islamic economics in the modern Muslim world operationalised only in the form of Islamic finance and banking institutions. Islamic economics and finance, in its current form, contrary to its claim, could not authenticate itself to be a novel system emerged from Islamic ontology, for it became a variant of mainstream economics and finance situated in the Western epistemological frame.

The modern and postmodern streams have also encircled Islamic economics such that Islamic economics does not allow differences in theory making and universalises itself through proposing its peculiar centricity and rationality assumptions, which methodologically does not differ from the mainstream economics, for it likewise takes nourishments from Eurocentrism and Western rationality – rejecting heterodox economic schools. A particular example of modernist convergence approach is the critic directed to the use of 'Islamic moral economy' instead of Islamic economics, as it is claimed that the use of Islamic economics is already satisfactory to meet the normative dimensions of an 'Islamic' economy, thereby there is no need to use another expression to define it. However, it is obvious that the term Islamic economics is a social construct evoking a particular branch of economics beyond being normative as essentialists suggests.[27] Thus, by the essentialist use of Islamic economics, it is alleged that there is only one economic system understanding, that is economics, and there is no way to define an Islamic economic system other than Islamic economics, which sounds like a by-product of 'the end of history' thesis by Fukuyama (1992). It is also a postmodern tradition that the divergence between economy and finance in the neoclassical economics has invariably been replicated in the trajectory of Islamic economics through the application of gradual 'financialisation of economy', which, in turn, cherishes Islamic finance through banking activities, while neglecting theoretical underpinnings of Islamic economics. Therefore, this fashioning leads to investing on Islamic financial education without locating moral philosophy at the core of banking and financial activities.

The concept of IME, due to these backlashes, has lagged behind in the Islamic economics literature as the mainstream was towards constructing Islamic economics and finance by embedding it into the neoclassical frame of economics without considering ontological and epistemological grounds in its theory making. Notwithstanding this, the concept is now yet to echo in the literature with the contributions of Asutay (2013, 2012, 2007a), Tripp (2006) and Utvik (2006). However, it should also be noted that the notion of IME still evokes nothing

[27] Here, the Islamic economics positioning meets the essentialist *vs* social constructivist debate in which the author takes his side with the social constructivist approach.

beyond romanticism in the perceptions of Muslim scholars since the prefix 'moral' does not imply being a part of moral economy understanding.

3.5.1. Islamic Moral Economy: A Conceptual Enquiry

Once IME is explained in the context of moral economy debate – beyond linking its morality to its Islamicness as the general claim suggests that 'if it is Islamic then it should be moral economy *per se*' –, the definition achieves its authenticity. Accordingly, Islamic moral economy can be defined as a particular system encompassing all other systems (political, social, cultural *etc*.) inside the Islamic order in which values and norms derived from Islamic ontology are embedded in the institutional framework and operating system. Therefore, in IME, human provisioning and interaction is submerged in a nexus of social relations beyond confining it only to economic relations by explaining everything around us with economizing behaviour in the sense of maximisation, efficiency and effectiveness. In this regard, society envelops its systems including economy by making them subordinated to the whole objective of achieving a good life or *hayat at-tayyibah* within the objective function of Islam aims to emancipate and empower individual.

IME, hence, aims to locate substantive morality into its economic theorising through constituting the substance of Islamic political economy, which functions under Islamic social formation as a framework by, hence, suggesting a particular mode of production, which, by definition, essentialises an Islamic norms-based production, consumption, exchange and distribution method. It also aims at bringing back the embedded nature of economy in the society by insisting on its constitutive moral norms and values that have determining and moulding roles over the institutional framework. In doing so, however, the re-embedding process in IME should not be identified with the Polanyian thesis of protective countermovement, albeit the concept of double movement is a good framework used by IME to explain social history and formation. This is due to the reflexive and protectivist features of countermovement that is contingent upon the existence of the *laissez-faire* movement. Therefore, in this respect, the centre determines the position of the subordinate, as self-regulating market in the centre necessarily creates social protection as a countermovement. IME, however, emerges as a counter hegemonic movement against disembedded character of the economy not with the purpose of social protection as the main objective, but rather treats re-embededdness in a self-proclaimed and proactive manner.

Having said that, it is also crucial to state that IME is not a pure economic, political, sociological or anthropological category that can be theorised to substitute mainstream economics or other sciences mentioned. It rather removes the artificial border lines of Western scientific categorisation of knowledge, thereby there exists no theoretically visible boundary lines such that each branch of knowledge becomes a constituent of IME. Thus, it is more appropriate to treat IME as an 'invisible economy', which constitutes the central idea of an embedded economy as explained by Booth (1994:654):

> … invisibility of the embedded economy. Invisibility means roughly that core aspects of the economy (division of labour, patterns of distribution, agent motivations and purposes) are so intermingled with noneconomic values and institutions as not to constitute a distinct theoretical sphere. More exactly, it suggests that because there are no theoretically visible boundary lines demarcating that realm from its surrounding social locus, "to speak of 'the economy' of a primitive society is an exercise in unreality. Structurally, 'the economy' does not exist. Rather than a distinct and specialised organisation, the 'economy' is something that generalised social groups and relations, notably kinship groups and relations do. … What we take to be an economic category is there charged with a plurality of unquantifiable, incommensurable functions, among which the economic function is never isolated and constituted as such; consequently, it has a determination that escapes the realm of the economy and so cannot constitute a part of an economic discourse.

As the economy becomes invisible through being embedded, there never appears distinct theoretical spheres, as evident in the modern Western thought, which interacts with each other only in an eclectic and instrumental way. Until then, moral economy goes beyond a subject area in which it is explained by 'individual subjectivity' – as sociologists popularized- or explained by 'social convention' – as anthropologists suggests.

3.5.2. Identity Formation in Islamic Moral Economy

As the foundational axioms set the framework of IME and provide its articulation in everyday practice, the debate on how Muslim identity is constructed and interacted with society in the IME framework brings important reflections on the degree of embeddedness and the practising norms and values in that society. In this respect, it is obvious that neoclassical theorists neglect social forces and structural regulation in shaping human actions, for they accept a mechanistic view of social progress which rests on the idea of methodological individualism and its accompanying generic notion of *homoeconomicus.* This notion does not allow any influence of social context or relations on human conduct; rather it essentialises individual and its actions without expanding the analysis to societal level. Similarly, behaviourists (*such as*: Skinner 1953; Watson 1926) relegate human behaviour to stimulus-response sequence whereby behavioural outcomes are considered to be controllable by analysing individual's motivational position, stimuli and environmental factors. Structuralists, *such as* Lévi-Strauss, (1971), on the other hand, takes an antipodal position to the previous ones by ignoring human potential and its agency role on the social context and change. Accordingly, structures determine human action by assigning no power to human agency.

In relating human conduct to social forces, IME adopts a totally distinct approach against the neoclassical, behavioural and structural positioning. In this manner, a Bourdieusian perspective helps to identify an action-based identity formation in the context of IME. In this perspective, Bourdieu (1985:724) states that society consists of some fields (workplace, school, friends, family, religious areas, political environment *etc*.), and, while entering these fields, individuals have their own habitus which is the space in which individual has some amount and type of resources and capital. Each field also has its own rules or '*doxa*', and once individual enters into the field, social groups and parties evaluate them through these rules and assign legitimate or illegitimate position for them. In rendering individual habitus and its negotiation with the field, Bourdieu's (1985) field theory argues that there is a two-way relationship in explaining human action and its intersection with social relations and forces. More precisely, human action is, in some degrees, adaptive to and embedded in the field, which allows norms and values to reflect in the behavioural outcomes. However, these actions are not entirely determined by social structures and forces, for the field itself is constituted by human capacity through its agency role, which enables reproducing past learnings in the form of new ideas and approaches for present and future situations of the field (for further debate on the field theory, *see*: Hanappi 2014:162). Therefore, while it is acknowledged that there is field effect on behavioural outcomes, human conduct has also constitutive role on the field through the dispositions of habitus that mediates field constraints and opportunities.

The bidirectional relationship is defined, in the Bourdieu's (1977) language, as 'structuring structures' and 'structured structures'. This definition necessarily brings power relations within the field at the centre of the debate. As, on the one side, human action is forced to be structured by external rules and social surroundings (structuring structures), humans also struggle for power to advance their positions in the field, which allows a continuous reproducing of field structure (structured structures). This power struggle, is shaped through bargaining, negotiating or co-opting by the stock of capital that humans hold in their habitus to improve their position in the field. The stock of capital varies in its kind including economic capital, social capital, technological capital, cultural and educational capital and organisational capital. As long as individuals can exert their power in the field with the capitals they stocked, they would able to strengthen their field struggle (Boyer 2008).

When individual identity, its formation and interaction is explained in IME framework with Bourdieu's field approach, an individual oriented *homoIslamicus* prototype is rejected as it evokes methodologically same approach with neoclassical notion of *homoeconomicus*. Therefore, it is more appropriate to transform *homoIslamicus* to an action-based identity. As now actions are considered within the context of its field, human conduct either conforms to each field's *doxa* (structured structures) *or* challenges it through individual habitus surrounded by Islamic norms and values (structuring structures). What IME aims to realize is that there should be continuous struggle to realise the Islamic axiomatic framework in each field through reformulating individual habitus with the aspirations of Islam and its way of life (*Shari'ah*) indicating Islam's 'becoming process'. Thus, one of the most important capitals that habitus should reserve is considered to be *ihsan* (beneficence for equilibrium) – the social capital through which each individual's *falah* or salvation is achieved, sustained and has implications for other's *falah* as part of *ihsan* process. Once *ihsan* (beneficence) is accumulated as a social capital – together with other forms of capitals –, individual habitus shapes the existing field structure by gaining more power, which in return, allows for redefining *doxa* in the light of Islamic axioms, including *tawhid*, *rububiyyah,* and *tazkiyah*, which then contributes to each individual's *falah* in the society.

If the whole objective, in individual level, is to be defined as reaching *falah* in this world and the hereafter through accumulating *ihsan* as social capital in the society, then the entire struggle evolves to become transforming past structures into an *ihsani* framework and also to preserve the *ihsani* structured structures against the *non-ihsani* forms of field structures. Yet, in this world, the tension between the establishment of *ihsani* and non-*ihsani* structures never ends, for each field is subject to power struggle, which keeps changing in the course of time. Therefore, IME defines the whole trajectory of establishing *ihsani* structure as a becoming process which can be defined as the never-ending search for betterment and which hence can only be completed in the hereafter.

As the action-based identity is adopted through Bourdieu's field theory, the methodological individualist explanations of human behaviour remain insufficient to evaluate how social forces intersect with human conduct. Therefore, the introduction of field theory contributes greatly to the embeddedness debate.

3.5.3. Instrumental Morality *vs.* Substantive Morality

As compared to the instrumental nature of moral roots of mainstream economic theorising, which mediates morality to perpetuate self-interested, utilitarian and pure economic goals, IME essentialises substantive morality to function and operate in its theoretical grounds and practical areas in an embedded manner. The difference between instrumental and substantive morality lies in their embedded character in the social formation of institutions and society overall. In particular to the experience with Islamic finance, this study argues that the moral dimension has been injected in the Islamic financial sphere only in an instrumental manner, which, in return, leads to no objection with the adoption of financialisation trend. In other words, while the temptations of prevailing financial system force its counterparts to establish no ethical authority over the functioning of financial system with the manifestation of self-regulated market understanding converging towards financialisation, Islamic finance would have made use of substantive morality to resist against disembeddedness in terms of subtracting moral character from the core of financial activities. However, the experience has so far demonstrated that morality has been instrumentalised through a form-based understanding of Islamic finance. This section, hence, presents the identification and exploration of instrumental and substantive morality that play an important role over the financialisation survey of Islamic finance.

Instrumental morality mainly rests on no ethical ground, and its conceptualisation corresponds to what Bauman (1994) states 'self-founding morality' or 'ethically unfounded morality' in our times. According to this, ethical principles in the postmodern period has been transformed into something that can only be validated and legislated in the hands of ethical experts, leaving no room for individual judgement for morality. Thus, when an individual faces ethical challenges, they leave their cognitions and reasoning aside and become 'expert-dependent individuals' (Bauman 1994:3), albeit in the pre-modern period we seldom need such ethical experts in our daily life. Islamic banking and finance (IBF) sector, and particularly the reliance on *Shari'ah* experts therein, is a good example evidencing the divergence between *fiqh* and morality as the outcome of instrumental morality. In this context, *Shari'ah* experts is situated in the *Shari'ah* boards of Islamic banks to be respondents and decision-makers of both *fiqhi* and moral challenges of contracts. As Islamic banking needs certain legitimacy in the form of compliancy from religious figures, who are 'ethical experts', to provide reconciliations against controversial issues of modern Islamic banking, while the moral consequences of contracts are neglected, for morality is considered only to be an instrument in the hands of *Shari'ah* experts who can decide on behalf of Islamic banking customers about the '*halalness*' of the contracts.

As evident, the surrendering and subordination of ethics to experts necessarily breaks the very link between ethical code and moral conduct. This disenchantment eventually breeds the ethically unfounded morality, or in our term, instrumental morality, which suggests that there is no reason or cause for being moral (or immoral), implying that ethical guidance and the attempts to legislate morality is a futile and blind hope. This overarching 'groundlessness' that postmodern moral theories impose on us melts morality in the autonomous society through instrumenting and dwindling its essence.

Substantive morality, on the other hand, challenges any form of instrumenting morality and its dissociation from ethical grounds, and claims an embedded nature of moral understanding, which covers an entire field including modes of production, social formation of society and institutional articulations of knowledge. IME, hence, essentialises substantive morality through its paradigmatic framework of political economy, value system, axiomatic approach and operational principles. In rendering its paradigmatic framework and value system, IME takes its nourishments from Islamic ontology, which defines ethical principles in its value proposition and aims to form Islamic value system and norms that constructs social structure. Ethically grounded Islamic moral values and norms are practiced, then, with the realisation of Islamic axioms.

Substantive moral foundations of IME necessitate a systemic understanding of political economy. In doing so, it develops, for instance, a critical approach to developmentalism, which is generally accepted as a moral responsibility of global economic powers to minimize injustice and smooth development. IME's critique to Western understanding and practice of developmentalism mainly rests on the idea that the roots of underdevelopment, poverty, unemployment, wars *etc*. stems from the socially constructed notion of 'development'. As contrary to its appearing, development has been instrumentally misused to convince people that it is a moral desire to emancipate humanity by providing maximum happiness through increasing material gain and consuming more. However, in fact, developmentalism transformed into something that every nation has to follow its path to flourish, that is why the so-called developed nations share modern way of life, the same economic systems and cultural habits through the effects of globalisation. It is for that reason, we are now moving from "universal modernity to globalised modernity" (Bauman 1994), where moral sense has lost its ground and became an instrument to produce pseudo-facts, as in the narrative of developmentalism.

3.5.4. The Crosschecking System: Contemplation, Intention, Action, and Consequence

The substantive morality is sustained through a crosschecking system wherein the complementary nature between contemplation, intention, action and consequence nourishes each other and enables to overcome form-substance dilemma in favour of the latter. In other words, the substantivity of moral character hinges on the coexistence of and harmony between each level. This also applies to the complementarity between morality and law; otherwise, any break in the whole chain (including morality and law) makes morality deficient and leads to a "shift from substantive morality to procedural rationality" (Tamanaha 2001:98). This is evident in the financialisation process through Islamic financial operations missing the consequential dimensions of transactions, whilst taking account of and satisfying with intention. However, as the axiom *tawhid* requires complementarity and unitarity between everything in the universe, this also applies in the behavioural aspect. In doing so, individuals start with contemplating (*tafakkur*) about their own soul, their physical environment, surroundings, and their relationship with the Creator as part of the 'knowing process'. However, contemplation has to lead an action (or 'doing process') (*see*: Panikkar 1973), since Islam never treats contemplative and active lives divorced from each other as seen in the monastic or ascetic lifestyles due to the fact that Islamic methodology is based on the articulation of *tawhid* or complementarity and unitarity in every aspect of life.

Between contemplation and action, there lies intention. Individuals intend to act in a certain way after their protracted or quick contemplations. Therefore, intention as an internal and silent phenomenon, and also definitive of actions (Powers 2015:43; *see* also Shaker 2013) is the outcome of contemplation that leads to trigger a particular action. Intentions accompany certain consequences if they realised into actions.[28] Thus, in general, contemplation precedes every other step and keeps its activity through a continuous functioning. In other words, a person contemplates and acts accordingly; but he still continues contemplating to judge whether his action meets his intentions and produce desired consequences.

Daily prayer in Islam is one of the best examples in rendering the harmonious relationship between these four constituents of the crosschecking system of IME: "Prayer, which in its highest form is contemplative and unitive, leads to salvation or deliverance of the soul from all bondage and imperfection and this in turn leads to correct action" (Nasr 1978:197). The act of prayer triggers contemplation at the end of which action is checked continuously until it serves

[28] For an effective debate on intention and consequence, yet from the Islamic management perspective, *see*: Fontaine (2008).

best to contribute to salvation and beneficence in individual and societal level. Thus, the *Qur'anic* verse (29:45) "Indeed, prayer prohibits immorality and wrongdoing" shows how daily prayer leads to prevent evil and essentialise good action through the process that starts with contemplation and culminates in consequence.

The complementarity nature of contemplation and action, together with the close relationship between intention and consequence, gain a distinct view to Islamic knowledge formation especially on nature; for individual contemplates on nature and its design, and then gradually objectivises it to understand and evaluate it in the best use of humanity. Through this, God's purpose over nature for the service of humanity and its ideal relationship with human beings becomes explored. However, modern scientific thinking drove a wedge between human beings and their nature (Nasr 1978:203); and the wedge is today even exacerbating such that modern human beings become alienated from their environment by causing environmental crisis, corrupting lands, destroying crops and animals.

The crosschecking system, elaborated above, helps create a substantive moral frame in reshaping Islamic financial operations, which so far have been relegated to contractual level analysis. Accordingly, newly developed products in Islamic finance industry were initiated with good intentions but were subjected to contract level analysis based on the considerations of *fiqhi* injunctions. However, the consequentialist evaluation of these products surfaced the dilemma between the prevailing constructed *fiqh* understanding and morality, in that the morally deficient outcome cannot be averted through the existing *fiqhi* knowledge domain. Thus, the crosschecking system developed in this section obviates such a dilemma by locating *tawhidi* methodology which asserts the unitarity and complementarity between intentions and consequences. Financialisation of Islamic finance, in this lens, reflects the failure to apply crosschecking system on the entire functioning of Islamic finance industry, mainly due to the societal outcomes caused by giving less importance to real economy related Islamic financial contracts that exacerbates the social disequilibrium and income inequality in the society.

The following section sheds light on the historical trajectory of Islamic finance and its applications from the perspective of Islamic moral economy with particular examination of normatively defined notions of substantive and instrumental morality, the crosschecking system and Islamic identity formation. Thus, it paves the way for evaluating the current trend in Islamic finance in an authentic manner beyond the aim of observing and explaining (or even justifying) the reality.

3.6. FROM ASPIRATIONS TO REALITIES: THE ISLAMIC FINANCE PROJECT RECONSIDERED

With the aim of elaborating on the notion of financialisation, its scope, and influence area, the literature on financialisation is surveyed thoroughly in the Section 3.3. By acknowledging the limitations of the existing debate, Section 3.4 expands it by introducing the Polanyian moral economy approach with the embeddedness discourse to gain a new insight on financialisation within the understanding of 'social formation of society'. As this study aims to explore Islamic financialisation and its social formational outcomes, IME is discussed in the previous section as a theoretical framework, which delineates the normative dimensions of Muslim financing, and hence critically argues the emergence of Islamic finance as a hybrid sector that mimics conventional financialisation pattern.

In explaining its theoretical boundaries, it is emphasised that IME emerges from Islamic ontology and aims to bring back the substantive morality to take root in its political economy framework, value system, axiomatic approach and operational principles. In doing so, it underscores the ontological differences in dealing with ethics and its moral outcomes, which, hence, shows the paradigmatic distinctiveness of IME. The value system, in the same vein, determines the framework and functioning of IME.

Although it has rarely been used in the relevant literature, IME considers itself to be a subfield under the general theme of 'moral economy'. Therefore, by nature, it addresses the issues around embeddedness, market economy, the positioning against anthropological and sociological interpretations of moral economy, and the identity formation that determines the role of human conduct in its interaction with social relations. In responding to these issues, as discussed, IME suggests a Bourdieusian approach around which identity is formed and the problem of embeddedness is transformed into a different sphere. In this, substantive morality is essentialised against instrumental morality. Further, the crosschecking system provides the entire process to achieve and sustain substantive morality.

The entire aspirational or normative dimensions of IME aiming to generate a system understanding beyond 'finance' and 'financialisation' as elaborated above, nonetheless, has not been possible to put into practice in an ideal sense in the modern times. Although Islamic economics was intended to emerge as a counter movement and an authentic reflection of counter hegemonic philosophy, the only institution emerged in the modern era has been IBF, which reflected a non-disruptive emerging pattern in spite of being disruptive of the existing modes of production and establishing an emerging science, in an aspirational sense. This section, therefore, aims to critically examine the nature of Islamic finance and its positional stance in the political economy framework of IME through identifying the financialisation tension in its financial transformation in the societies it operates as part of the emerging disembeddedness and social formation debate.

It is important, in this manner, to explore first the socioeconomic and political circumstances, which has influenced the emergence and global diffusion of Islamic banks and evolution towards Islamic financialisation; thereby potential sources of its developmentalist failure and disembeddedness can be broadly comprehended through critical examination of its initial objectives by introducing financialisation as an important aspect of hybridity of Islamic banking.

3.6.1. Islamic Finance: A Post-colonialist Project

The emerging need of an Islamic financial system had surfaced in the late 1940s when decolonisation took place after the World War II. With this new stage of political history, previously colonised countries are allowed to design their own institutional structure without any political interference of colonial powers. From inner perspective, Muslim societies' confrontation with the existing social, cultural, political and economic articulations of Western worldview has now been transformed into a different phase where direct applications of Western hegemony were interrupted after the decolonisation.

While boundaries of these lands were no longer invaded by Western colonialist powers and the ways of democratisation and nation building are expedited and 'liberalised', old colonial legacies were still prevailing and shaping social and economic structure of these underdeveloped world. Thus, it caused a particular form of dependence that was conceptualised with 'neo-colonialism' – a term coined by Nkrumah (1965) – under which the former economic and cultural relationships of direct colonisation period are maintained through different means in disguise of economic cooperation, global culture, development *etc*. Islamic finance project, in this circumstance, was intended to play an important role in authenticating Muslim nation building through advantages of decolonisation by providing financing for development constructed through Islamic political economy aspirations. However, it had to come up against the prevalent economic structure in following years of its establishment.

3.6.2. A Search for an Authentic Muslim Identity

With the nation building process after the colonial period, an authentic Muslim identity was aimed to construct in the face of rationalist, individualist, secular and capitalist features of homogenising global identity. By forming the new identity, in macro perspective, it was expected that the old colonial legacies would be overwhelmed eventually by recalling and reconstructing Muslim legacies, which was also envisaged to decrease the contingence upon Western entrepreneurship in the economic activities in Muslim lands. Islamic finance was essentialised, outside the scope of colonial mind-set, to help generating social welfare and becoming a panacea for economic development in the long term.

In order to face with the unrivalled system of economics inherited from the colonial era, first underlying critiques were concentrated around the issue of prohibition of *riba*, since its elimination from the existing economic systems in Muslim countries was also considered to be an important part of the whole objective of renewal in Islamic economic thought in the sense of constituting (new) Islamic political economy. Accordingly, Muslim scholars in the modern period, especially Mawdudi (1986), Qutb (1976) and Quraishi (1974), proposed a distinct alternative to capitalist economy primarily with the motivation of elimination of *riba*. While Mawdudi (1986) and Qureshi (1974) mainly constructed their argument around *riba* and its prohibition, Qutb (1976) was stressing on the immediate need for establishing social justice in resurging Islamic developmentalism. However, Mawdudi's attention was more on behavioural aspects of societal change. Accordingly, his argument was that economic rules itself remain incapable of establishing an Islamic order; therefore, individuals should keep a strong moral sense to ignite societal development. As *Qur'an* strictly prohibits *riba*, since it produces injustices between different stakeholders in the Islamic modes of production, financial activities are believed to be maintained without interest so that '*ihsan*' or equilibrium can be achieved between all the involved stakeholders whereby the dominance is de-centred (Asutay 2018).

With such an initial aspiration, the number of Islamic banks has proliferated and spread out significantly in a few decades as part of the objective of authenticating alternative mode of financing after the first commercial Islamic bank in 1975. By the institutionalisation of Islamic banking, it is expected to maintain economic activities in an ethically or Islamically driven industry wherein trading in real assets is prioritized against artificial financial products and a *Shari'ah* governance structure is employed inside the bank to avoid potential exploitative relations between financier and borrower.

The factors of forming an authentic Muslim identity and pursuing a non-interest based financial system had found its chance to be practiced in the Muslim states of Pakistan, Iran and Sudan. These countries organised their constitutions around fully-fledged Islamic principles including economic system and put their endeavour on the idea of Islamic economics to practice in the real world. It is for this reason that a great degree of theoretical studies in the literature of Islamic economics are contributed by Pakistani and Indian scholars. More precisely, the related publications that are written in English and Urdu language by Pakistani and Indian intellectuals and academics constituted bulk of the entire literature until 1990s (Philipp 1990).

Iran, similarly, challenged the mainstream economic theorising and transformed every institution into Islamic ones including conventional banks. The project of Islamic finance in Iran, with these improvements, was seen an important tool for recourse to 'good old times' (Taleghani 1983). However, it was overlooked that the real challenge was to maintain *Shari'ah*-compliant financial activities in an 'Islamic' country in the decade of highly globalised multipolar world financial system. In order to bring back the 'good old times' in this stage of history, there must be a back-shift in the social formation of societies, which is, in fact, impossible to conduct or realise. Instead of this romanticised view, a totally distinct social formation should be envisaged to emerge in this era in which Islamic norms and values are embedded in the economic system and economy is subordinated to whole society's emancipation.

3.6.3. Economic Impact of Oil Crisis in 1973 on Islamic Banking Growth

If the dynamics of establishing Islamic banks are linked with certain motivations, pursuing a *riba*-free financial system can be considered as religious motivation, while forming a distinct Muslim identity would be a mix of social, cultural and political motivation. Although one cannot think of a pure economic reason for the emergence of Islamic finance, a highly substantial politico-economic factor is the 1973 oil crisis, which accompanies political and economic consequences for the entire Muslim geography. Standing at the middle of a series of energy crises between 1967 and 1979 in the Middle East, the oil price rise of 1973 – from $3 per barrel to $12 – (Macalister 2011) and the subsequent embargo was a decision given to punish the USA and the West as a response to their support of Israel in the Yom Kippur war against Egypt. After the embargo, large amount of oil revenue flew into oil-wealth countries of Gulf states, which is known as 'petro-dollars', put into economic cycle of oil exporting countries through three different ways (Saeed 1996:11):

(i) by buying Western consumer goods, military hardware, industrial equipment and other goods;
(ii) by investing their funds in development projects at home and abroad;
(iii) by lending money through official and private channels to oil-less countries.

King Faisal of Saudi Arabia played an important role, at that time, on cutting down the foreign control of global financial powers around the local oil industry in the Gulf region by channelling the idle funds (petro-dollars) into the benefit of financing needs of business sector. In line with this, King Faisal encouraged the establishment of Islamic banks through funding them by oil-linked wealth (Abdul-Rahman 2010:193; Saeed 1996:11). Therefore, one can conclude that Islamic finance was initiated mainly owing to the presence of oil money; otherwise it would have postponed its leap to late times, albeit the religious motivation was there to support.

Acknowledging the importance of dramatic rise in oil prices and its significant impact on the establishment of Islamic banks, one can critically approach to this argument by claiming that the early contributions to the idea of Islamic finance and its initial applications had no link with Arab petro-dollars (Ahmad 1987:7) if one looks at the first banking examples in Malaysia's Tabung Haji (1967), Egypt's Mit Ghamr (1963) and Nasser Social Bank (1971), none of which was funded by oil money. As the cases of Mit Ghamr and Tabung Haji is explained in the next section, this claim has no significance once it is recognised that almost all Islamic banks established in 1970s was partly or totally funded by oil money or facilitated by the expansion of oil monies. This means that the main catalyst for the emergence, diffusion and expansion of Islamic banks is associated with the oil factor in 1973 (*see*: Imam and Kpodar 2013; Imam and Kpodar 2010). The initiatives of interest-free operations mentioned above, are individual and local attempts, which is far from reaching a generalisable idea.

3.6.4. Wider Political Economy Factors Encompassing the Emergence of Islamic Finance

As the preceding discussion clarifies the emergence of Islamic finance had taken its expansion and global diffusion from the religious concern of *riba* and the economic and political environmental restructuring in the post-colonial period. The initial attempts on operationalising a type of *riba*-free banking system is mostly referred by the special experiments of Mit Ghamr social banking and Tabung Haji saving institution. In fact, prior to these, there were some other micro level cases such as the loan cooperatives in Indian subcontinent in 1940s, or a particular form of *riba*-free credit network in Pakistan in late 1950s (Warde 2000).

3.6.4.1. Tabung Haji and Mit Ghamr

Tabung Haji, basically functioning as Pilgrims Savings Corporation in Malaysia, was established in 1963 to help prospective pilgrims in performing their pilgrimage (*hajj*) through accumulating their savings. Thus, it has functioned as an investment project or company. Mit Ghamr, similarly, was a kind of savings/investment bank that was founded in 1963 by Ahmed al-Najjar. Inspired by German saving banks, Mit Ghamr succeed in mobilizing small savings from the rural areas of Egypt to create small amount *riba*-free loans to be used in productive areas through extending financing to small entrepreneurs. It also introduced the investment accounts on the basis of profit sharing. By appreciating these novel experiments, it is, however, hard to convince that the igniting motive behind the idea of Islamic finance is mainly derived from the operations of these two institutions, for they neither give explicit reference to religion in their activities nor become a part of certain Islamic movement (Haniffa and Hudaib 2010:86). Mit Ghamr, aimed only to uplift economic conditions of the poor in the small region by introducing profit-sharing model, and did not envisage a long-time project of spearheading Islamic banking model. Another evidence, in the sense of them being non-systematic initiatives, is that they never considered to carry out commercial banking activities, which was essential to expand the industry. Contrary to the vested understanding, this study claims that all the previous experiments, in fact, encouraged people about the possibility of constructing a systematic formulation of Islamic banking that can be applicable within conventional financial system. In other words, it demonstrated that economic issues in the modern world can still be dealt under *Shari'ah* compliant ways (El Ashker and Wilson 2006).

3.6.4.2. Petro-dollars and pan-Islamism

Systematic construction of the frame of Islamic banking gained momentum in the aftermath of oil crisis, which also triggered the pan-Islamist strategy by King Faisal. Together with Nasser's project of establishing Nasser Social Bank (1971) as part of the objective of unifying Arab world against the impositions of Western (neo)-colonialism (pan-Arabist ideology) and particularly of gaining Islamists' sympathy against leftist groups in Egypt, King Faisal, likewise, organised regular gatherings for Muslim countries in the wake of the oil crisis to create a 'consciousness on unity' under the sacred objective of Muslim *ummah*. Later on, with these gatherings known as Organisation of the Islamic Conference (OIC), they came up with the idea of establishing Islamic Development Bank (IDB) in 1974. Subsequently, the first non-governmental Islamic bank was founded as Dubai Islamic Bank (1975) as a commercial bank. Based on their funding with petro-dollars, Islamic banks proliferated all over the Muslim region between 1970s and 1980s, such as Kuwait Finance House (1977), Faisal Islamic Bank of Egypt (1977), Faisal Islamic Bank of Sudan (1977), Jordan Islamic Bank for Finance and Investment (1978), Bahrain Islamic Bank (1978), and International Islamic Bank for Investment and Development in Egypt (1980), Bank Islam Malaysia Berhad (1982), Tadamon Islamic Bank (1983) and Sudanese Islamic Bank (1983).

Through these developments, other early pioneers played a major role in boosting the number of Islamic banks through negotiation between businessmen, finance and banking professional, *Shari'ah* scholars, regulators and statesmen. Amongst them, Sheikh Saleh Abdullah Kamel, a Saudi businessman, and Prince Mohammed Al-Faisal founded respectively Al-Baraka Group and Dar Al-Mal Al-Islami (Khan 2017). As an overriding rational for its augmentation, Islamic banking was appealing to many parties to be a tool for spreading the idea of pan-Islamic identity, while some perceived as an opportunity to diversify their portfolios.

Despite the economic conditions were satisfied by the presence of oil money in enhancing Islamic banking activities and hence spreading pan-Islamist ideas under the guise of resurging Islamic developmentalism in the Muslim world, the practical aspects of applying a non-*ribawi* banking system in a highly globalised financial world has so far demonstrated that there were many problems within the operations of Islamic banks in the sense of their conforming to *Shari'ah* rules and moral outcomes. Although Islamic law embraces basic principles regarding financing and a bulk of historical financial experiments were accessible to reach, the urgent need of establishing Islamic banks did not allow to deal with its theoretical underpinnings in a sophisticated way. Instead, the moral and legal challenges faced in the sector were met 'reflexively' and 'pragmatically'. From the perspective of public policy makers, Islamic banks had to proliferate to provide alternative ways of financing *vis-à-vis* mainstream finance. Therefore, its theory was relegated to secondary importance and redefined with the necessities of the industry.

Adopting this approach, of course, posed some critiques on practitioners from legal and moral aspects. While the contracts were criticised, from a legal perspective, for their resemblance to conventional financial contracts, which violates some *fiqhi* principles, or even, in some contracts, harbouring *riba* component, the industry was also inculpated with its immoral consequences that violates the notion of social justice and Islamic developmentalism.

3.6.4.3. Universalising conventional finance

By appreciating these critiques, however, the main sources of developmentalist failure of Islamic finance should be approached from a wider perspective by considering its religious and political economy determinants – mentioned above – under the umbrella of the social formation of societies. In this sense, it is essential to recognise how Muslim societies are forced, in the capitalist period, to form their social and economic relations subservient to financial interests of the capitalist system. Accordingly, the entire relations are relegated to and explained by economics terminology. For instance, people are believed to reflect 'economising behaviour' in their interpersonal relations, such as maximising their utility, thinking rationally and keeping their self-interest motives alive. Therefore, from individual and social aspect, morality is considered out of the context of economic life. Economic relations, hence, do not necessarily predicate on ethical principles and likewise produce moral outcomes. Instead, price mechanism is considered to be the sole determinant of social equilibrium and justice.

Islamic finance, in such a construct, should renounce the objective of integrating into global financial system by mimicking conventional way of financing; instead, it should make use of the experiences and applications from the actual history of Muslim societies. However, contemporary Muslim scholars' delusion and insist upon the observed mimicry emanates primarily from their naïve understanding, which identifies conventional way of banking as a value-neutral financing activity. In fact, conventional banks are value-loaded financial institutions implying a redesign towards disembedding existing institutions in the service of economic objectives. Further, as stated by Azarian (2011:262), these banks were "never stripped of moral dimensions and constraints", implying that a universal understanding of finance immune to changing social factors in different societies is not admissible. Thus, the attempts to offer an alternative to conventional banking system out of the aspirations of Islamic economics should focus on reaching authenticity in establishing a development oriented financial system beyond mimicking conventional financial structure. Otherwise, once the structure is taken for granted, authenticity in Islamic finance will never be reached; but rather hybrid institutions will emerge as evident in the sector (*see*: Hall 1992:310).[29] It should also be stated that attaching social objectives to Islamic banks as an emotional reaction without embedding them into the core of Islamic finance does not make these banks 'Islamic' in real sense; as the 'institutional logic' (*see*: Thornton and Ocasio 2008) of conventional banks

[29] "People belonging to such cultures of hybridity have had to renounce the dream of ambition of rediscovering any kind of 'lost' cultural purity..." (Hall 1992:310).

shaped by the capitalist worldview such as the objectives which essentialise shareholder value maximisation and 'capital' as the hegemonic factor of production will inevitably be transferred into Islamic financial sphere.

Mentioning that the expected authenticity has never been acquired in Islamic banking, its reflexive and market-dependent characteristics have shown parallels with the changes in the global political and economic dynamics. In this regard, the collapse of oil prices and the rise of liberal economic policies in the 1980s made Islamic banking more decentralised, deeply market driven, pragmatic and diverse. In the 1990s, where the new world order had been settled through Washington Consensus, politicians used Islamic banking as part of financial liberalisation as a tool for exerting political power and legitimating the dubious financial activities through state-dependent *fatawa* councils. At its state of art, throughout the trajectory of Islamic finance, it can be summarized that the sacred intentions are perplexed with secular goals (Haniffa and Hudaib 2010). Amongst its potential identifications, as Pollard and Samers (2007) argue, Islamic banking and finance could neither be an articulation of alternative economy nor of moral economy, but something hybrid influenced by the varieties of capitalism.

The main influence, within the varieties of capitalism, is the financialisation phenomenon, which transformed the nature of finance as an everyday practice into something with which substantial changes in the goal of economic activities accompanied. According to this approach, finance is no longer considered to be a tool for improving individual's capabilities and functions through enhancing economic performance, but the aim with the financialisation process is rather to employ an opportunity space, independent from the objectives above, where various incumbents, pressure groups and rent seekers aim to 'financiate' and 'commodificate' values and things through various financial institutions (multinational companies, stock markets, banks and *etc*.) and instruments. The following subsection, accordingly, provides a general picture under which financialisation of Islamic finance as the underlying cause for the developmentalist failure is considered.

3.6.5. Islamic Finance: Disembeddedness and Financialisation

Beyond its neoclassical interpretation within Islamic economics discourse, considering the emergence and progress of Islamic finance from moral economy perspective entails to treat Islamic financialisation as one of the repercussions of modernist social formation of Muslim societies. Thus, rather than being a matter of fact, the proliferation and global diffusion of IFIs heralds the disembedded character of economies in the Muslim dominated countries, implying the neglect of Islamic social formation and substantive morality in the financial sphere by sustaining the entrenched principles of neoclassical economic paradigm in its framework. The incorporation of Polanyian debate, hence, circumvents limitations of the existing perspectives on financialisation, which fits and can only explain the historical trend of mature economies at most whilst falling short of bringing a new dimension to the new economic orientation in the rest of the world.

Despite the conceptualisations such as ‘subordinate financialisation’ (Lapavitsas 2013) or ‘peripheral financialisation’ (Becker *et al.* 2010) crystalize the actual role of finance in developing economies, it only represents the contributions of such economic structures to the whole process of financialisation in the advanced economies. The internal dynamics of financial ascendance in the peripheral economies, however, cannot be explained with the existing approaches in the financialisation literature. As explained in detail above, Islamic finance, for instance, has subordinate and peripheral character in terms of its strong affinities with conventional financial structure; nevertheless, the aspect that locates Islamic finance within the context of financialisation is rather related with Polanyian debate of social formation and double movement.

As reiterated in the previous sections, such a transformation of Muslim economies in the modern period has complied with the requisites of neoliberal economic paradigm. In this sense, the emergence of Islamic finance converged into Islamic financialisation over time, and necessarily produced a hybrid sector due to its failure in authenticating Muslim financing in line with the aspirations of IME. This assertion has also been examined through country case studies, where Islamic finance is systematically gaining significant importance in the national economy, however, at the same time, evolving into financialisation trap by following the global financial trend. Among scarce resources on the subject matter, Rethel (2010), in reflecting on the trajectory of development of Islamic finance in Malaysia, associates the rise of Islamic finance in Malaysia with financialisation of Malaysian economy. As Malaysian capitalism has been sophisticatedly evolving into financialisation stage through the development of capital markets, financing patterns -both conventional and Islamic - engendered a new politics of debt together with a sharp transformation in financial relationship, which ushered in the emergence of financialisation embedded in local structures and institutions (Rethel 2010:503). The previously state-led investment activities, amid this development, started to give way to quasi-market capitalist initiatives through the dominance of financial investment. Islamic finance, in such an atmosphere, plays an intermediary role in bridging the state-led and market-pushed phenomenon of neoliberal financialisation (Rethel 2010:503). Similarly, Rudnyckyj (2013,

2017) critically examines the recent developments in Malaysian economy and associates them with the global neoliberal policies. Accordingly, the development of Islamic finance in Malaysia was first projected in the 1980s to create a Muslim middle class through envisaging a new identity formation (Rudnyckyj 2017:279). By doing so, financial inclusion policies accompanied with the integration of indigenous Malays into the national economy whereby Malaysian state has facilitated "the shift from financial inclusion to the construction of a new Muslim entrepreneurship in 2000s" (Rudnyckyj 2017:274) based on the neoliberal values that has been embedded in the financial sector through fashioning the debt-based instruments of Islamic finance. This process, on the other hand, elicited a new form of Islamically designed market reason and economic rationality understanding in the minds of Muslim Malaysian entrepreneurs (Rudnyckyj 2014:110). Financialisation process in Malaysia through Islamic finance, therefore, is closely linked with the political aspirations of Malaysian state to create an economic understanding resulting into neoliberal Islam.

Similar to Malaysian case, the rise of financialisation in the 21st century Turkish economy was addressed by Apaydin (2015) with special focus on its impact on philanthropic activities of conventional and Islamic banks in Turkey. It was argued, hence, that the government led by Justice and Development Party (AKP) politically motivates and incentivises new Muslim business elites to involve in non-state social service provisions in return for allocating profitable financial investment areas primarily to these privileged groups, so that philanthropic activities would pave the way for political returns in the long-run (Apaydin 2015:461). In doing so, as Apaydin (2015) argues, Islamic banks also take part in this process of financial ascendance by increasing their role in the financial sector. Thus, as she identifies, while on the one hand financialisation rises in Turkish economy through the collaboration of political incumbents and financial constituency, Islamic banks are also given privileged position to play a contributory role on financialisation with a stipulation of engaging in philanthropic activities.

While the state of art, including Malaysian and Turkish cases, evidences quite opposite, it was expected, originally, that Islamic finance would constitute a counter hegemonic alternative to the mainstream finance, for it aimed at essentialising equity-based financing, profit and loss sharing, risk-free returns and participatory investment alternatives to create collaborative, cooperative and shared environment in the financial sphere. By doing so, the commodifying logic of mainstream economics was aimed to be overwhelmed with particularly introducing the Islamic notion of *ihsan*, which ultimately aims to decommodify land, labour and money in a Polanyian sense to establish equilibrium in the society beyond justice by helping those who have not achieved to reach certain level of human well-being.

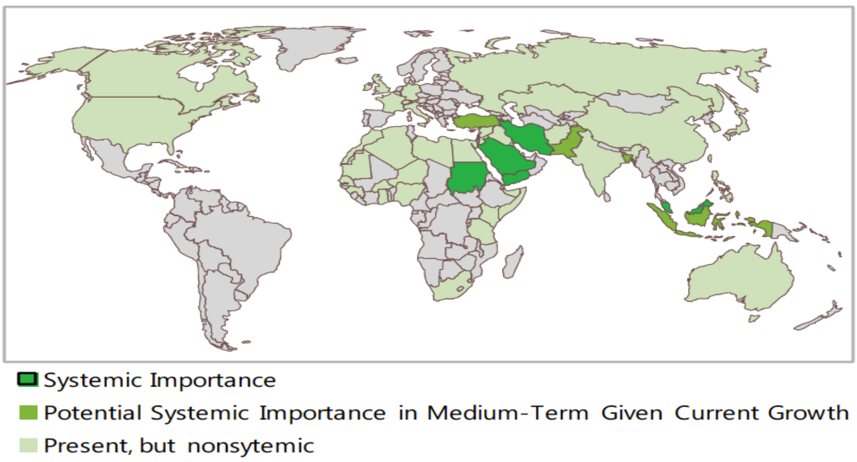
3.7. LOCATING FINANCIALISATION IN ISLAMIC BANKING AND FINANCE: AN EMPIRICAL EXPLORATION

The preceding sections elaborated on the theoretical construction of embedded nature of Islamic finance and also the observed dis-embeddedness through financialisation in the sector through a critical discursive analysis in a comprehensive manner. This subsection, subsequently, aims to render empirical analysis by witnessing the practical aspects of Islamic finance as a financialising activity within Islamic economics paradigm. Prior to this, first, a descriptive analysis is provided to depict the current state of the industry from the aspects of size, scope, segment orientation and market share. Statistical data, then, are utilised to evidence the observed financialisation taken place within Islamic financial sphere by looking through its asset structure, the sectorial distribution of financing, and outstanding modes of finance. Lastly, an empirical analysis is conducted to evidence how Islamic finance engenders a financialised view of Islamic economics through its operations.

3.7.1. Financial Performance of Islamic Banking Sector

The latest developments in the industry demonstrate that Islamic finance attracts significant attention, with its promise of being an authentic mode of financing, in all over the world especially in the wake of global financial crisis of 2007 wherein an undoubted confidence on mainstream financial system that heretofore is weakened remarkably. In revealing a snapshot of its permeation area in the globe, Figure 3.1 shows the changing degrees of systemic importance of Islamic finance in various parts of the world.

Figure 3.1: Islamic Finance Markets by Systemic Significance



Source: IMF Staff Discussion Note (Kammer *et al.* 2015:13)

It is obvious in Figure 3.1 that Islamic finance, albeit still in its infancy, has managed to diffuse along many parts of the world except South America. In particular, Islamic financial markets hold systemic significance in Brunei, Iran, Malaysia, the GCC countries, the Sudan, and Yemen; while in other parts of the world such as North America, North Africa, Eastern Europe, Asia and Australia it has potential systemic importance in the medium term. It can, therefore, be deduced that Islamic finance has diffused all over the world rapidly in a short span of time and has been securing its position in different regions.

Behind the objective of diffusion rest the idea that economic development would necessarily essentialise finance as a catalyst for economic growth, a claim that echoes mainstream approach to financialisation. In this regard, both Islamic and mainstream views avoid questioning the role given to finance and its function within economy; hence prefer concentrating on financial development regardless of its socioeconomic consequences. Figure 3.1, hence, reflects such an essentialised view of finance-centred development despite the fact that IME aims at de-centring finance through its counter hegemonic character.

Table 3.2: Selected Key Institutional Players

Commercial Banks	Al Rajhi Bank, Bank Maskan, Kuwait Finance House, Bank Mellat, Maybank Islamic Berhad, Bank Melli Iran, National Commercial Bank, Dubai Islamic Bank
Standard Setters & Regulators	Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI), Islamic Financial Services Board (IFSB), International Islamic Liquidity Management Corporation (IILM), National Regulators, International Islamic Financial Markets (IIFM), Islamic International Rating Agency (IIRA), Liquidity Management Centre (LMC), General Council of Islamic Banks and Financial Institutions (CIBAFI)
Takaful	Etiqa Takaful Bhd, The Company for Cooperative Insurance, Syarikat Takaful Malaysia Bhd, The Mediterranean and Gulf Cooperative Insurance and Reinsurance Co., Islamic Arab Insurance Company (Salama), Takaful Ikhlas Sendirian Berhad, BUPA Arabia for Cooperative Insurance
Microfinance & Crowdfunding	Al Amal Microfinance, Alhukwat (Pakistan), Shekra, Kiva, Yomken
Islamic funds	SEDCO, BIMB Arabesque, AlAhli Saudi Riyal Trade, Al Rajhi Capital SAR Commodity, International Trade Finance Fd (Sunbullah SAR), Amana Growth Fund
Waqf	AlRajhi Endowment. Awqaf Saudi Arabia, Awqaf South Africa, Awqaf and Minors Affairs Foundation (AMAF)
Sukuk Arrangers	Emirates NBD, CIMB Group, Standard Chartered PLC, HSBC Holdings PLC, Saudi National Commercial Bank, National Bank of Abu Dhabi, Maybank
Education & Research	INCEIF (International Centre for Education in Islamic Finance), Islamic Research & Training Institute (IRTI)

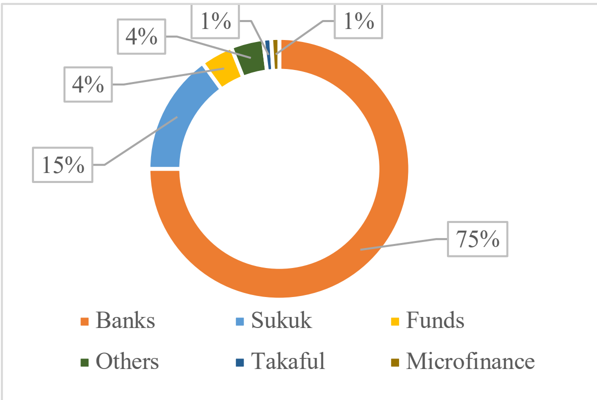
Source: Compiled from ICD-Thomson Reuters (2015, 2016); Askari *et al.* (2011), Asutay (2015)

The spread and systemisation of Islamic finance has accompanied with institutionalisation process and hence proliferated the number of Islamic banks, regulatory bodies, standard settings, educational units and research studies (Asutay 2015). Accordingly, Table 3.2 shows a selection amongst the key institutional players within Islamic financial industry that emerged over time for dealing with the disputed issues in the grey areas created by hybrid nature of Islamic financial system. Looking exclusively on standards and regulations, it is seen that

Islamic finance keeps mimicking its conventional counterpart in designing a control mechanism strengthened with such standards and regulations that are framed in the global financial structure. Furthermore, it overlooks the fact that this frame is constructed against potential risks of financial crisis during the financialisation process. Therefore, the objective with designing such standards and regulations in the case of conventional financial system is to pursue pro-finance economic policies against the threats of chronic financial crisis. This assumption is taken for granted in Islamic finance without any consideration, but differently, the industry endeavours to justify it through its shallow *fiqhi* reasoning.

As banking and insurance activities play a major role in conventional financial system, similarly, Figure 3.2 depicts the composition of the Islamic financial services showing the dominance of Islamic banking sector, where Islamic banks lead the entire sector with enjoying three quarters of the total industrial assets, and *sukuk* follows it with a share of 15%, looking promising for the future. This emanates from the peripheral character of Islamic financialisation, which depends entirely on banking sector to pursue financial activity.

Figure 3.2: Composition of Global Islamic Financial Services Industry



Data Source: Dubai Centre for Islamic Banking and Finance (DCIBF) (2015); Ernst & Young (E&Y) (2016)

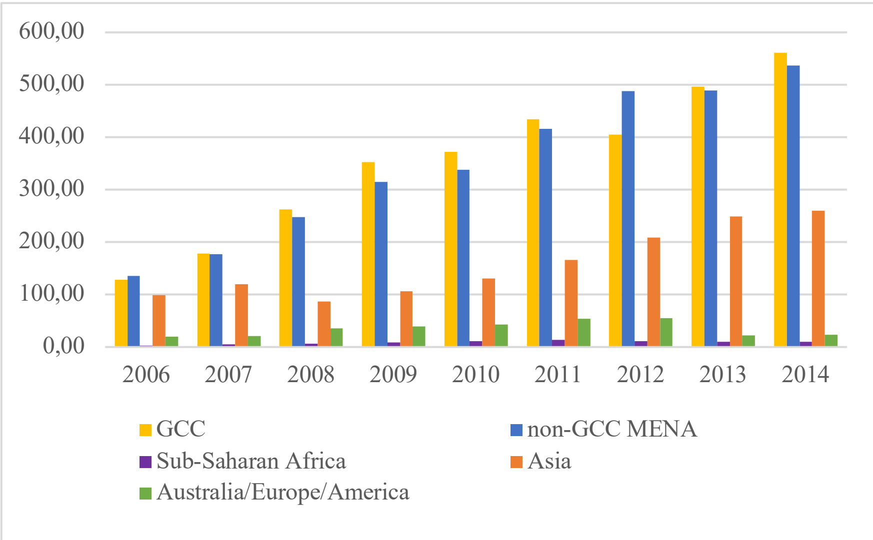
Bank based development of Islamic finance industry is also evident in both regional (*see:* Table 3.3, Figure 3.3 and Figure 3.4) and national (*see*: Table 3.4 and Figure 3.5) statistics. In the year 2015, for instance, the asset size of each segment, shown in Table 3.3, brings the GCC into forefront with heavy concentration on banking activities, while *sukuk* is gaining considerable importance in Asia with its proximity to banking asset size (US $182.7 and US $218.6 respectively). Figure 3.3 also confirms that the GCC have been leading the industry - mainly due to the oil wealth as elaborated in the previous section, and MENA region follows it closely. Southeast Asia has also gained significant momentum in furthering Islamic finance activities primarily with leading roles by Brunei, Malaysia and Indonesia.

Table 3.3: Breakdown of Islamic Finance Segments by Region ($US in billions)

Region	Banking Assets	Sukuk Outstanding	Islamic Funds' Assets	Takaful Contributions	Total
Asia	218.6	182.7	19.8	4.4	425.5
GCC	650.8	115.7	23.4	11.7	801.1
MENA (exc. GCC)	540.5	16.6	0.2	841	565.7
Sub-Saharan Africa	26.6	1.9	1.5	0.6	30.6
Others	56.9	2.1	11.2	-	70.2
Total	1493.40	318.5	56.1	25.1	1893.10

Source: IFSB (2017)

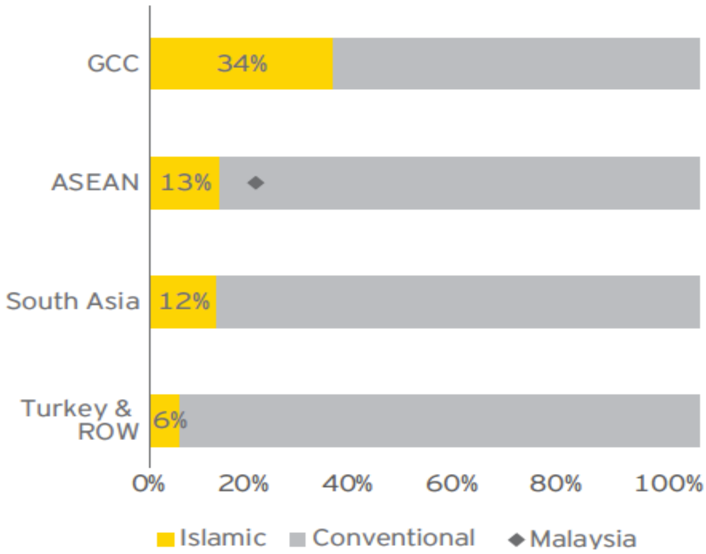
Figure 3.3: Regional Islamic Banking Assets Size ($US in million)



Data Source: The Banker (2014, 2015, 2016)

In Figure 3.4, the comparison between Islamic and conventional banks in terms of their asset size within regions unveils the fact that the scope of Islamic banking is not sufficient yet to compete with conventional finance. However, Islamic banking asset size in the GCC and Asia, 34% and 13% respectively, is expected to reach a considerable level and gain an edge over its conventional counterpart in the long run.

Figure 3.4: Regional Share of Islamic Banking Assets



Source: Ernst and Young (E&Y) (2016:10) (*ROW: rest of the world)

In the national level, the asset structure of various countries is shown in Table 3.4 with the percentages of each Islamic finance segment within a specific country. It is noteworthy to underscore that the dominant Islamic financial institution is banking in most of the mentioned countries with its share in the total Islamic finance sector ranging between 78% and 99%. Thus, the rest of Islamic financial service providing institutions can be considered as infant. However, Islamic banking in Malaysia and Indonesia has relatively medium level asset size with respective shares of 41.9% and 53.8%, where *sukuk* seems to be burgeoning to claim a large share.

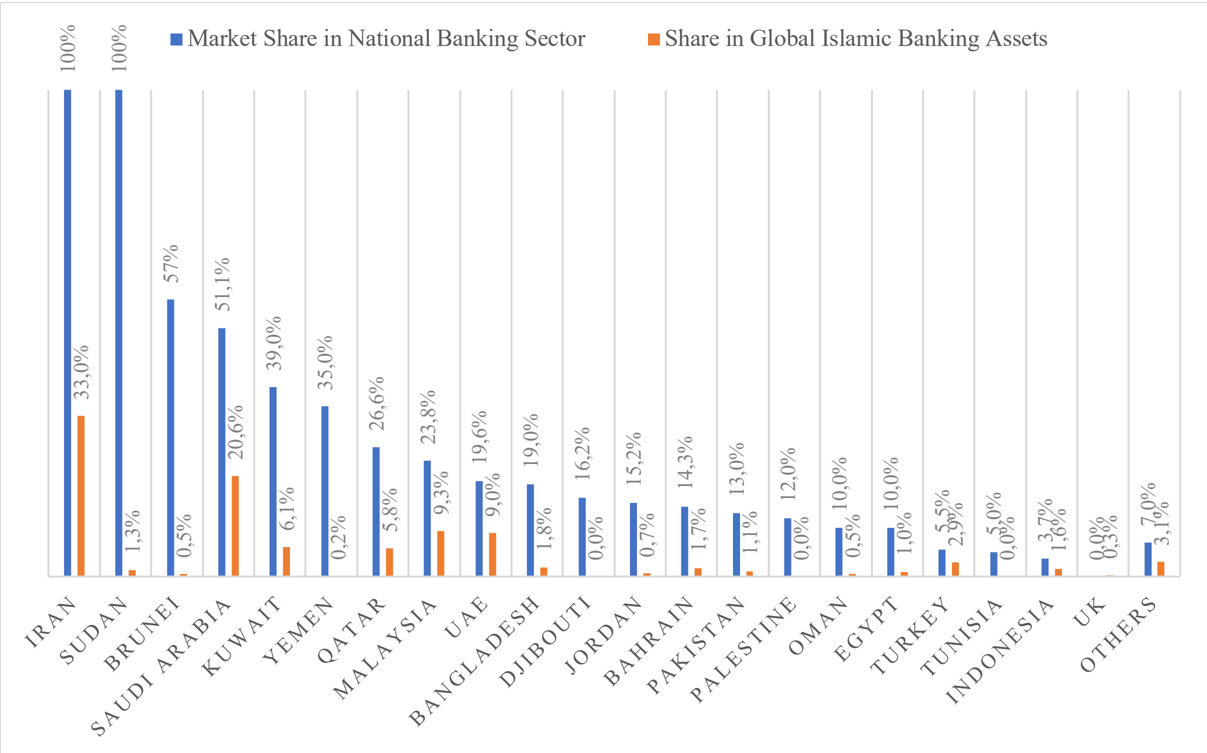
In order to acknowledge its impact in national and global level, each country's share of global Islamic banking assets, and the market share of Islamic banking in total national banking assets are given in Figure 3.5. The regional concentration of Islamic finance on the GCC and MENA is also reflected here in the national scope, for the leading figures of the industry come from most of the oil reach countries with their high shares. Nonetheless, Malaysia, Indonesia, the UK and Turkey hold potential in leading the industry in the long-term, since their industry growth does not depend upon the oil factor, and more prominently, two different percentages of these countries in the figures are proportionally proximate to each other, implying that Islamic banking has relatively intense in the whole share of national banking sector.

Table 3.4: Islamic Finance Asset Structure at National Level (in %)

	Islamic Finance Assets	Islamic Banking Assets	Takaful Assets	Other Islamic Financial Institutions	Value of Sukuk Outstanding	Islamic Funds Assets
Saudi Arabia	100	78,39	3,18	1,79	11,66	4,99
Iran	100	87,40	2,42	6,35	0,94	2,90
Malaysia	100	38,61	1,77	9,53	45,54	4,55
UAE	100	79,22	1,11	2,99	16,40	0,28
Qatar	100	83,61	0,53	0,73	14,89	0,23
Kuwait	100	85,84	0,19	11,67	0,88	1,42
Bahrain	100	92,62	0,46	0,98	5,92	0,02
Turkey	100	80,63	0,00	0,00	19,35	0,03
Indonesia	100	42,15	2,66	1,57	51,93	1,70
Bangladesh	100	97,12	2,55	0,32	0,00	0,00
Pakistan	100	68,22	0,79	11,76	13,18	6,05
Egypt	100	96,59	0,00	2,04	0,00	1,37
Sudan	100	99,10	0,39	0,52	0,00	0,00
Jordan	100	95,53	1,32	1,78	1,27	0,08
Global	**100**	**72,43**	**1,88**	**5,31**	**17,07**	**3,32**

Data Source: ICD-Thomson Reuters (2016)

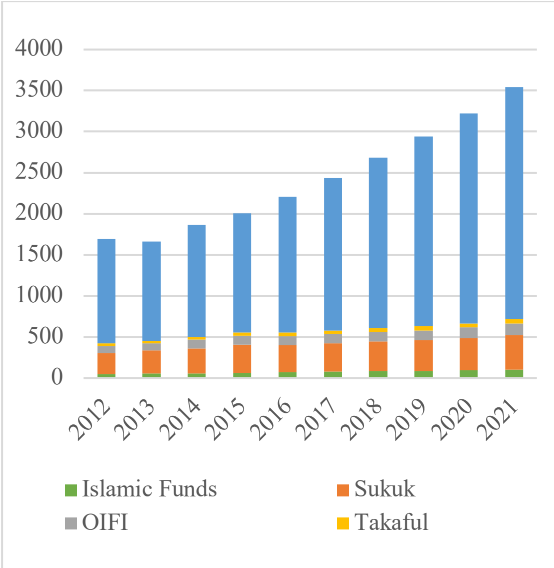
Figure 3.5: Shares of Global Islamic Banking Assets and Market Share in National Banking Sector



Data Source: IFSB (2017); Dubai Centre for Islamic Banking and Finance (DCIBF) (2015); Ernst and Young (E&Y) (2016)

Along all these developments, it seems that the weight of Islamic banking in the overall Islamic finance industry will be much higher in a couple of years, as shown in Figure 3.6 with the asset size growth of each segment for the last four years with a projected growth until 2021.

Figure 3.6: Global Islamic Finance Assets by Sector Growth (US$ billion)



Data Source: ICD-Thomson Reuters (2016)

As evident in the descriptive analysis in this section so far, the historical trajectory of Islamic finance embraces a considerable mimicry with conventional finance and its operational framework, which basically centres banking activity at the core by adopting debt-based financing with less consideration of contributing to real economy and neglecting the objective of social financing. In this regard, Islamic finance, too, follows the pattern of financialisation with its own idiosyncrasy, and instrumented its foundational aspiration of 'profit and loss sharing' at the expense of efficiency ethos.

3.7.2. An Analytical Examination of Financialisation of Islamic Banking

After critically examining the growth of Islamic finance sector within the global financial system through touching upon its global, regional and national records, this subsection aims to explore the institutional structure, organisation and operations of Islamic finance, and examine them within the context of financialisation that is dealt in six categories above. In doing so, it investigates as to what extent and through which ways Islamic finance meets the characteristics of different financialisation perspectives.

It should be stated, at the outset, that the essentialisation of Islamic finance beyond the Islamic economics paradigm is indeed a clear and initial sign of Islamic financialisation, wherein financial sphere has exclusively gained an autonomous and constitutive role over the functioning of Islamic economic institutions, thereby Islamic financial development is objectified as the indispensable prerequisite for achieving economic development, an argument that has roots in the neoclassical framework of financialisation. Such an essentialist conduct is inherited from the mainstream approach of financialisation, which similarly stresses financial development in advancing global economic performance. Therefore, both views adopt a positive attitude towards the rise of finance and finance-centred understanding of economy by neglecting societal consequences of the process of disembedding finance from economic realm.

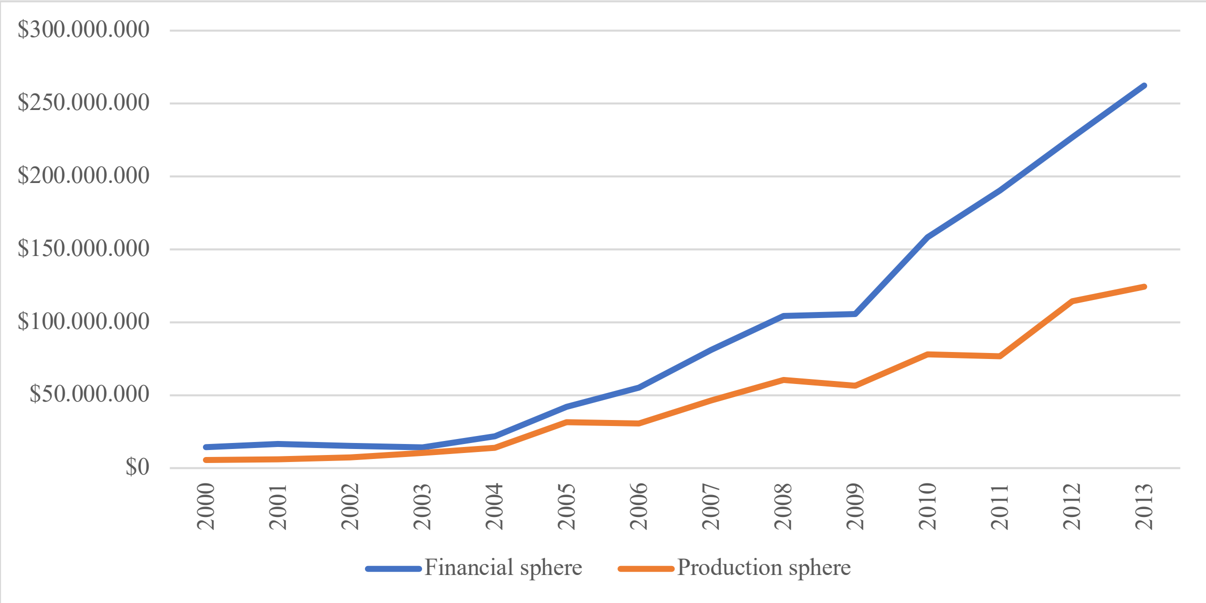
Contrary to the positivistic approaches towards financial ascendance, Krippner's (2005) definition of financialisation unravels an important aspect of financialisation of Islamic finance. Accordingly, the consideration of financialisation "as a pattern of accumulation in which profits accrue primarily through financial channels rather than through trade and commodity production" (Krippner 2005:174) is reflected, to a certain degree, in Figure 3.7, which illustrates the distribution of global Islamic financing to production and financial sector. It is evident in Figure 3.7 that Islamic banks' funds primarily flow is directed towards financial sector. Despite the trajectory of development depicted in Figure 3.7 does not render global Islamic banks' profits derived from financing different sectors, hence does not directly fit into Krippner's content, it still helps to draw some important inferences for Islamic financialisation, since Islamic finance similarly strengthens financial channels rather than real economy by putting most of its financial services at the disposal of financial sector.

Besides Krippner's (2005) emphasis on 'profit' aspect in delineating financialisation, post-Keynesian theorists' focus on poorly performing 'production' post-Keynesian sector in the face of the expansion of financial sector crystallises another important dimension of financialisation of Islamic finance. In this respect, Figure 3.7, again, illustrates the divergence between financing of financial sector and production sector[30] by global Islamic banks over sampled period of 2000-2013. The significance of divergence starts with the year 2005, and by suffering from the nightmarish times of the global financial crisis, the gap between the lines representing financial and production sector widens even further with the values of financial sphere doubling

[30] While financing banks and financial institutions, consumer durables, and services are considered under financial sphere; financing the sectors of agriculture, manufacture and trading is opted for production sphere. For the discussion whether to categorise consumer durables under financial sphere, see the explanation provided in footnote 36.

that of production sphere in the last few years. Confirming the post-Keynesian claim, it is clear in the figure that financing production sector by Islamic banks falls into stagnation during the expansion of financial sector's financing.[31]

Figure 3.7: Financing by Sectors, Production and Financial, Islamic Banks Global, 2000-2013 (in US$ thousand)



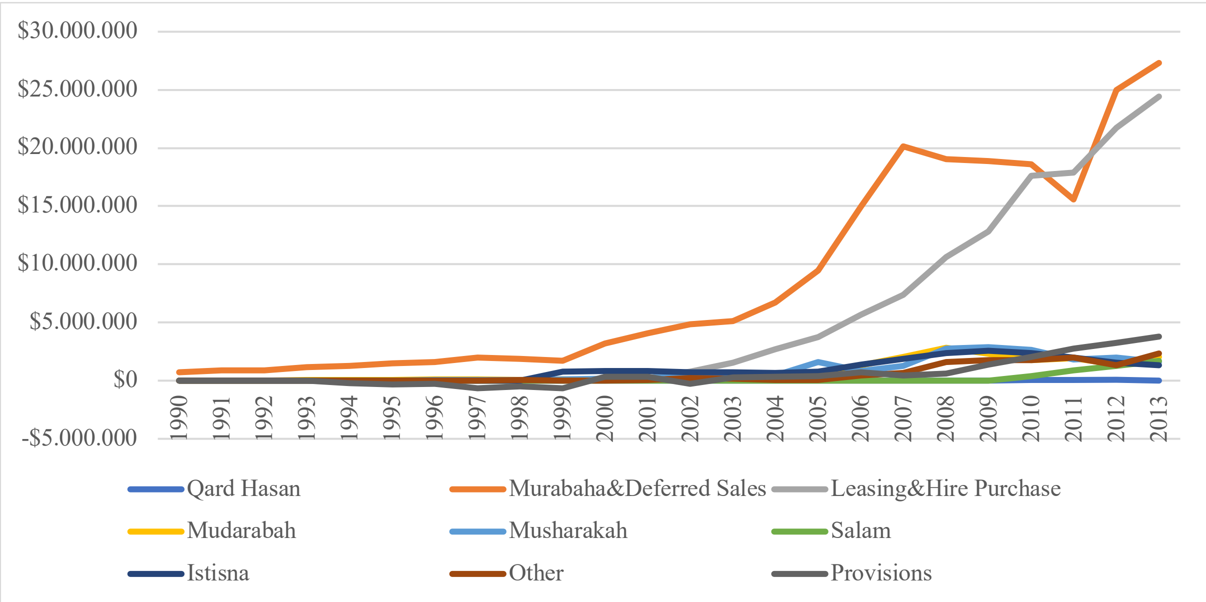
Data Source: Islamic Banks and Financial Institutions Information, Ibisonline.net/IRTI

The shrinking of production sector in conventional economic systems is due to relative decline of deriving profits therein, hence financial sector has shined out as an alternative sector to invest for higher profitability. This necessarily accompanied with short-term oriented financial investment against investing on long-term projects in the production area. In the Islamic side, a similar process is observed in the concentration of financing modes. Accordingly, despite participation based long-run contracts, such as *mudarabah*, *musharakah*, and *istisna,* are ready to invest to fulfil profit-and-loss sharing and risk-sharing natures of Islamic finance, *murabahah* (and to some extent *ijarah*) contract and recently *tawarruq* are adopted as a short-term and relatively less risky trust-based mode of financing. With this, Islamic banks derived relatively higher profits with involving short-term debt-based financing alternatives (such as *murabahah*, *tawarruq* and *sukuk*), and hence avoid the burdens of participatory contracts as they are mostly long-run projects and embrace various financial risks albeit their return is proportionally high and stimulate real sector and productivity. In rendering some evidence, the nature of Islamic financing modes of (i) United Arab Emirates, Qatar and Saudi Arabia from

[31] Unfortunately, the data between 2013 and 2016 is not available in IRTI's website; hence we cannot show the latest trends. However, our expectation is on the side of further widening of the gap.

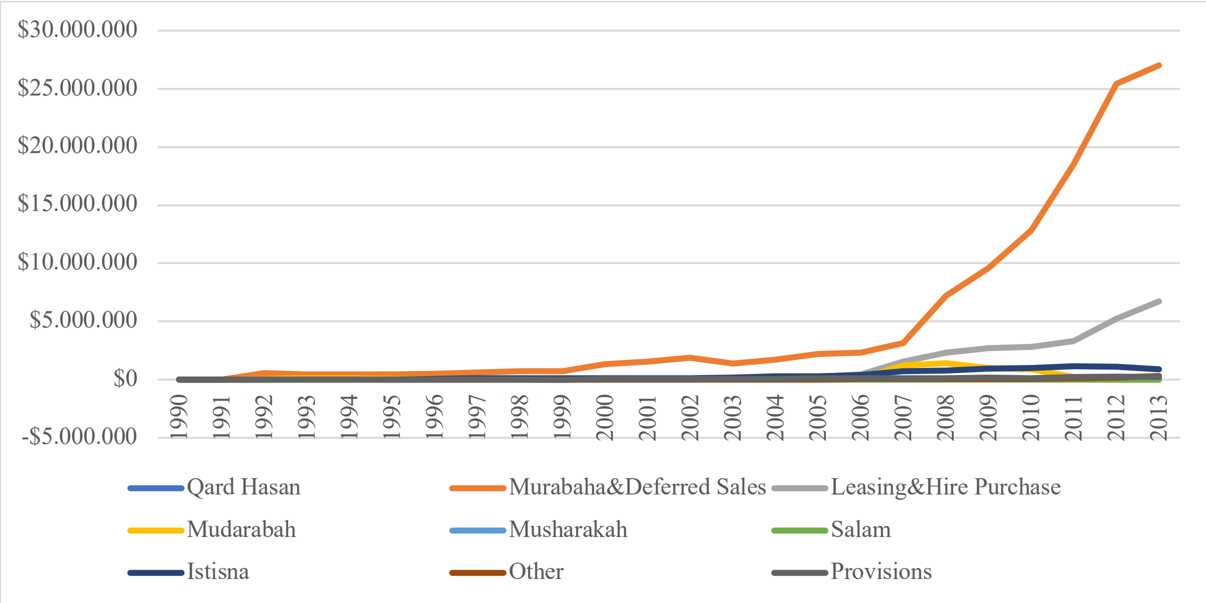
the Gulf Region (in Figures 3.8, 3.9 and 3.10), (ii) Pakistan, Bangladesh and Malaysia from the South Asia (in Figure 3.11, 3.12 and 3.13) are shown as short-termism and financialisation evidences, which invariably favour *murabahah, sukuk* and *ijarah* type fixed income Islamic financial contracts in their operations. Islamic banking in Indonesia, however, follows a different pattern by bringing the long-term oriented and profit-and-loss sharing natured financing of *mudarabah* and *musharakah* to the fore. Despite *murabahah* stays as an inevitable fact therein, 'other' labelled mode of finances also preserves significance; however, what constitutes 'other' financing modes is not disclosed. This is presumably related to the fact that there are different micro level financing modes widely used in Indonesia, hence cannot be incorporated into the analysis as a different category.

Figure 3.8: Islamic Modes of Finance by Islamic Banks in United Arab Emirates, 1990-2013 (in US$ thousand)



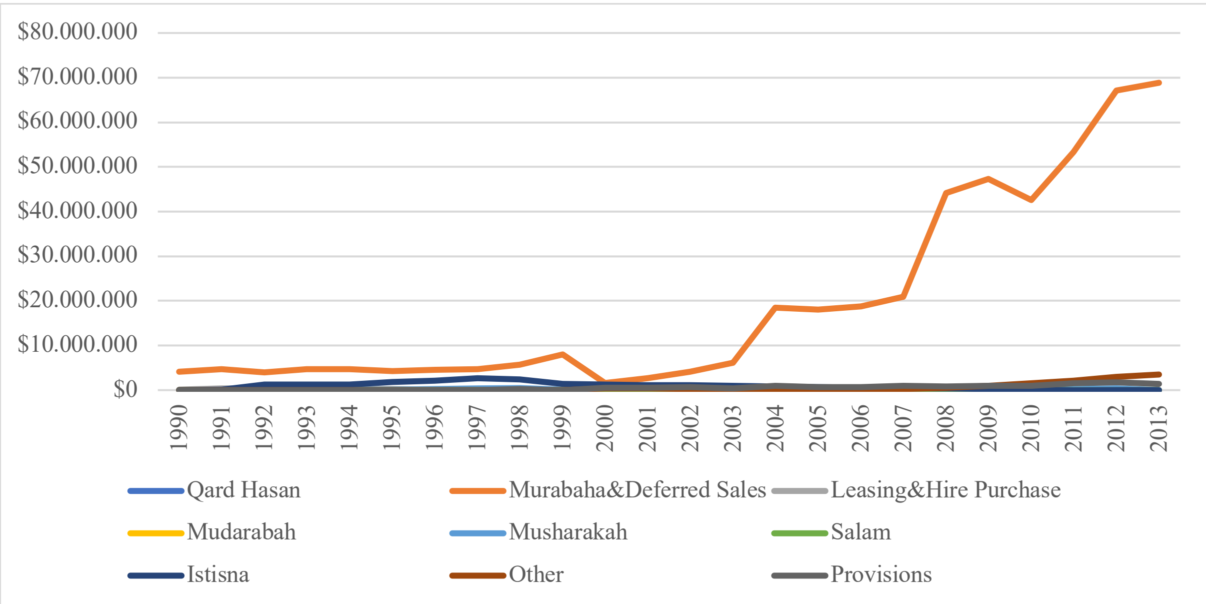
Data Source: Islamic Banks and Financial Institutions Information, Ibisonline.net/IRTI

Figure 3.9: Islamic Modes of Finance by Islamic Banks in Qatar, 1990-2013 (in US$ thousand)



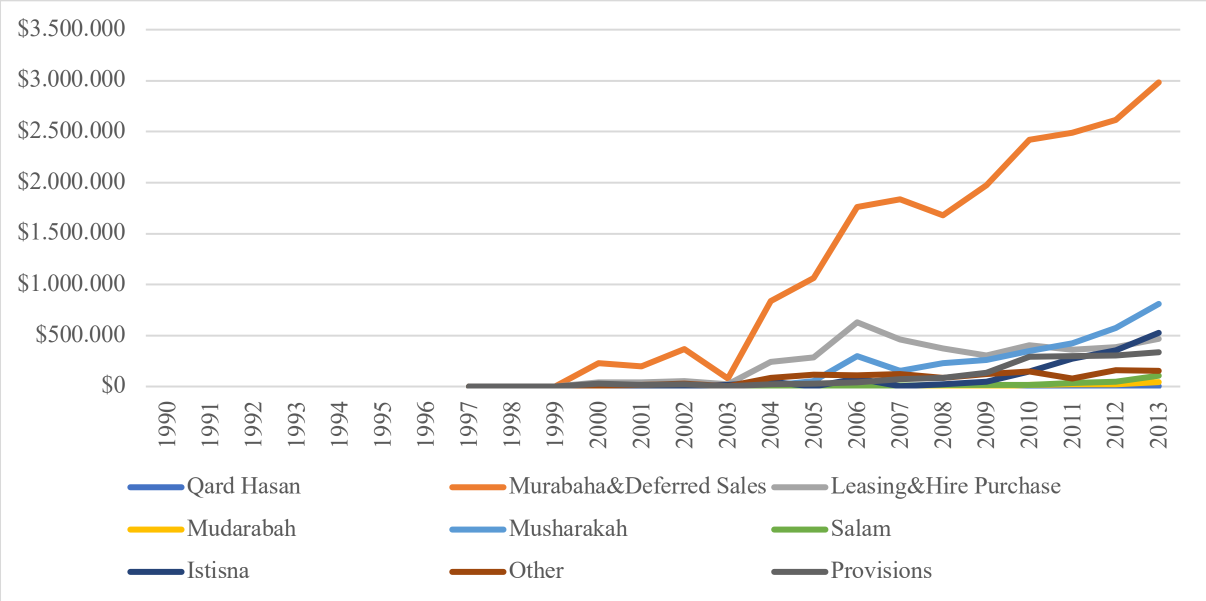
Data Source: Islamic Banks and Financial Institutions Information, Ibisonline.net/IRTI

Figure 3.10: Islamic Modes of Finance by Islamic Banks in Saudi Arabia, 1990-2013 (in US$ thousand)



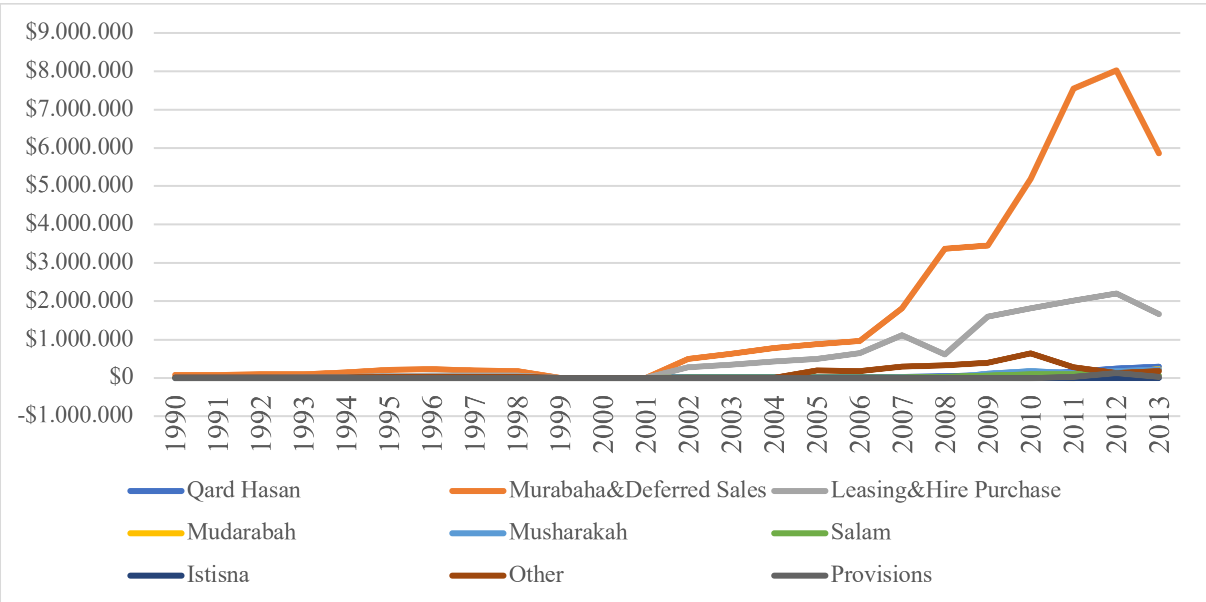
Data Source: Islamic Banks and Financial Institutions Information, Ibisonline.net/IRTI

Figure 3.11: Islamic Modes of Finance by Islamic Banks in Pakistan, 1990-2013 (in US$ thousand)



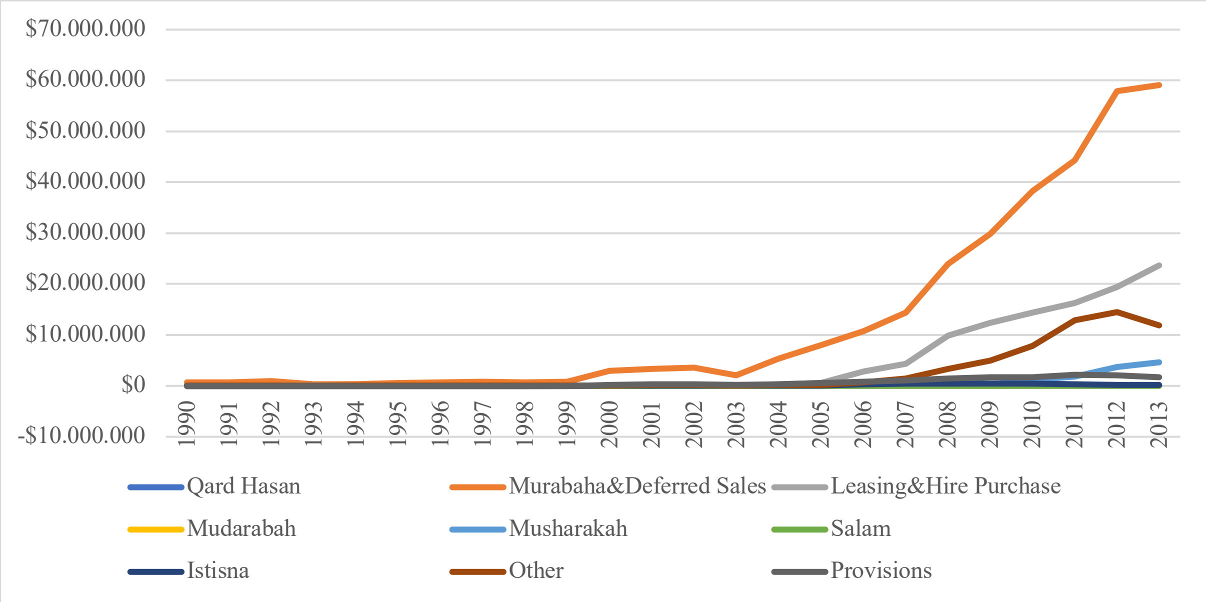
Data Source: Islamic Banks and Financial Institutions Information, Ibisonline.net/IRTI

Figure 3.12: Islamic Modes of Finance by Islamic Banks in Bangladesh, 1990-2013 (in US$ thousand)



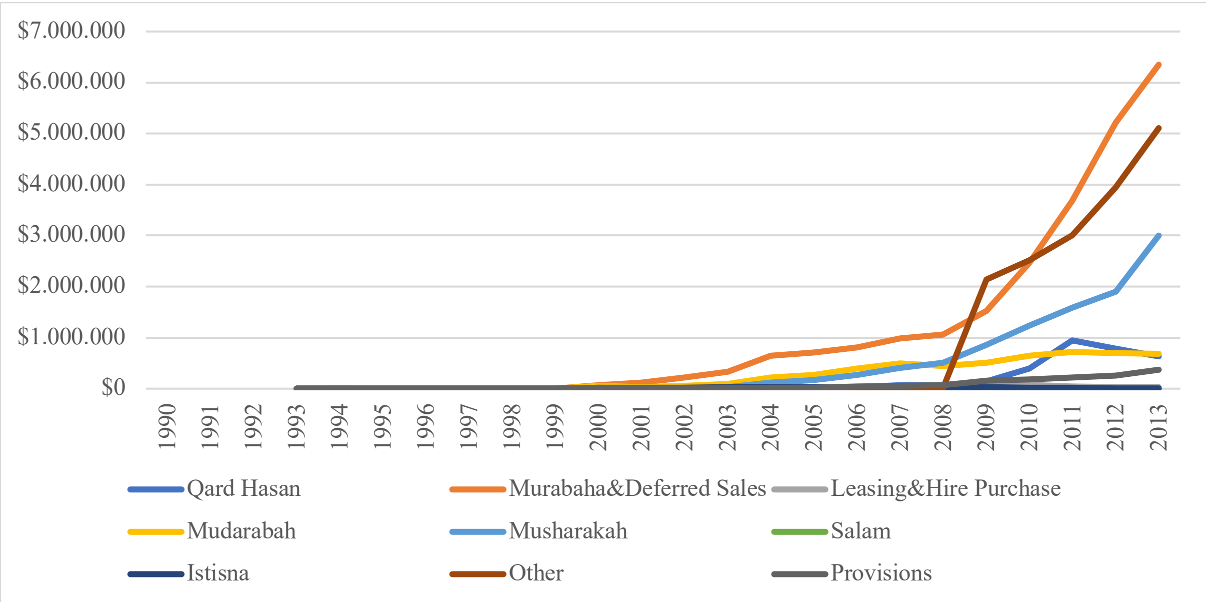
Data Source: Islamic Banks and Financial Institutions Information, Ibisonline.net/IRTI

Figure 3.13: Islamic Modes of Finance by Islamic Banks in Malaysia, 1990-2013 (in US$ thousand)



Data Source: Islamic Banks and Financial Institutions Information, Ibisonline.net/IRTI

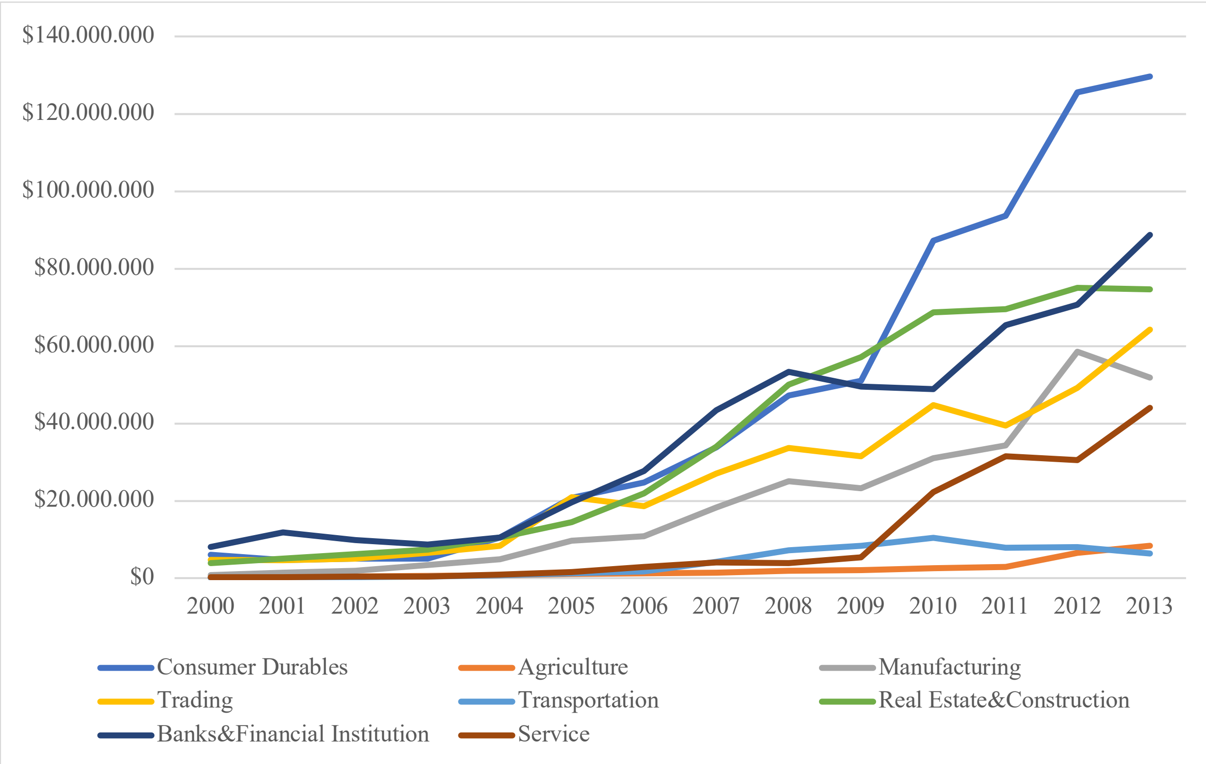
Figure 3.14: Islamic Modes of Finance by Islamic Banks in Indonesia, 1990-2013 (in US$ thousand)



Data Source: Islamic Banks and Financial Institutions Information, Ibisonline.net/IRTI

Acknowledging that Indonesian Islamic financing practice as a rare exception within the general trend, it can be claimed broadly that banks, in the new international economic setting, diversify their profits mainly through (i) increasing income shares from client services within service oriented activities (payment services, expertise, advice, asset management) (Dembinski 2009:46); (ii) borrowing (mortgages, general consumption, education, health); and (iii) expanding financial assets (housing, pensions, insurance, money market funds) (Lapavitsas 2011:620). Receiving its share from the new banking profile, Islamic banks similarly reorient their interest to these fields. Figure 3.15, accordingly, demonstrates the significant rise of financing service sector, consumer durables, real estate and construction, banks and financial institutions. It is, therefore, clear that Islamic banks have complied with the new international financial setting by adjusting themselves with the new structure through mimicry and hybridisation leading to financialisation.

Figure 3.15: Financing by Sector, Islamic Banks Global, 2000-2013 (in US$ thousand)



Data Source: Islamic Banks and Financial Institutions Information, Ibisonline.net/IRTI

The convergence of Islamic finance towards conventional financial system does not confine itself with the banking area. In this regard, the rise of Islamic capital markets[32] (Islamic funds, sukuk *etc.*) constitutes another dimension of financialisation of Islamic finance. Following the coupon-pool capitalism approach of financialisation, capital markets' simple role of intermediation between household savings and investing firms in the productionist form of capitalism transformed into a new structure wherein capital markets regulate both household and firm behaviour through coupons. In the same vein, Islamic capital market instruments are getting dominant in the sector with the neglect of their shady aspects in terms of conforming

[32] The size of major Islamic capital market instruments is shown in Figure 3.2, where the share of *sukuk* and Islamic funds totally reaches around 20% of total Islamic financial industry. Long-term projection in Figure 3.6 proposes that the growth of Islamic capital markets will continue in the future as well.

to the *Shari'ah* principles, since the nature of these instruments does not differ much from the conventional capital market instruments. Thus, the convergence towards adopting debt-based financing is consolidated even further through Islamic capital markets,[33] and fictitious transactions have taken place through 'Islamic coupons' such as *sukuk* issuance, Islamic unit trusts, and Islamic mutual and investment funds. Muslim households' income and *Shari'ah* compliant firms' wealth are, therefore, pulled along the financial sphere in the form of Islamic coupons.

Last remarks and some empirical support can be given to the position of financialisation of Islamic finance through the distinguishing concept of 'subordinate' financialisation. Lapavitsas (2013) argues that the subordinate character of developing countries' financial systems traces back to 1970s, in which financial liberalisation was commenced as the new international economic policy that aimed at trade openness across borders. Washington Consensus of 1979 aimed at liberalising economies and financial sector, later in the 1990s, cemented this policy by suggesting domestic economies to welcome international capital flows so that capital in rich countries would flow to the poor, and hence expedite their economic development process. In this regard, the export of capital from developed to the developing economies increased in the form of foreign direct investment (FDI) and the entry of foreign banks in the domestic economy (Lapavitsas 2013:245–46). However, in fact, a reverse capital flow has been generated from developing to the developed economies, thereby poor countries' economic conditions were even worsened at the expense of strengthening financialised capitalism through capital exploitation.

The implications of subordinate financialisation over Islamic finance are seen in opening Islamic windows at the conventional banks and the leading role of the UK as the new Western hub for Islamic finance. Capital transfer from domestic economies is mostly conducted through Islamic window banking (hybrid banks) and the London Metal Exchange (LME) to channel 'Islamic capital' into the international financial system (for further information on the role of the LME on Islamic banking practice and operations, *see*: Schoon 2016).

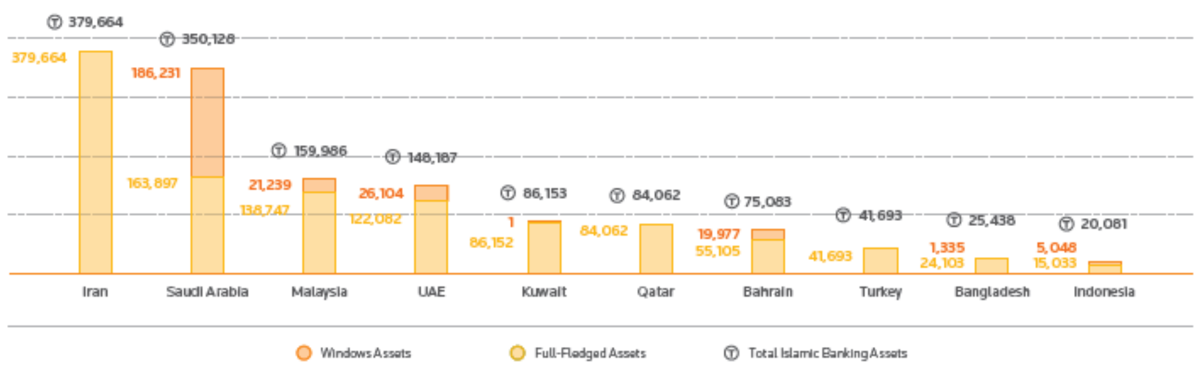
Despite the triad of Iran, Saudi Arabia and Malaysia running the biggest and largest Islamic finance markets, London aspires to get involved in the triad and to increase its share through

[33] When *sukuk* market is analysed with sectors, it is seen that the funds raised by the financial services industry (30.96%) and government sector (42.87%) accounts for almost 74% of the total issued *sukuk* (see Chart 1.3.1.7 in the IFSB Stability Report 2017:20). Similarly, asset class breakdown of the global Islamic funds shows that money market (25%) and equity (43%) hold 68% of the total Islamic funds (see Chart 1.3.2.8 in the IFSB Stability Report 2017:26).

issuing Islamic financial alternatives. LME plays a pivotal role in this in extracting capital from developing Muslim countries by offering a platform for Islamic banks' liquidity management. Considering its size and operating fields worldwide, LME takes advantage of its monopolistic power and hence easily dominates Islamic finance industry by functioning as the major merchandise allowing its traded commodities to be used by Islamic banks globally. As the Islamic financial contracts must be backed by certain asset in principle to provide credit on it, commodities traded on LME are used to show as the underlying asset in such transactions. Thus, most of the commodities in Islamic contracts including commodity *murabahah* and *tawarruq* are referred to those traded on LME (Wigglesworth 2014). The function of LME benefits significantly in flowing Islamic capital into the UK, since it remains the only source for global Islamic finance. In recent years, Dubai, Luxemburg, Hong Kong and South Africa started to challenge the UK's position by offering alternative platforms for *murabahah* and *tawarruq* trading in order to make a grab for some of the business (Torchia 2014); however, London still preserves its privileged position thanks to the LME.

The flow of capital from developing world to leading developed countries, in the case of Islamic finance, is also sustained with Islamic window-based hybrid banking system, which aims to derive capital gains from Islamic finance industry that reaches nearly $2 trillion, a great potential for the financial world in crisis. The latest statistics depicts that the assets of IFIs by Islamic window banking amount 18% with the value of $284,785 million while fully-fledged Islamic banks enjoy 82% with $1,310,398 million (ICD-Thomson Reuters 2016:38). Figure 3.16 illustrates how Islamic windows within conventional banking system masses in the pioneer countries such as Saudi Arabia, Malaysia and UAE. Both statistical records together with the substantial role of LME evidence capital transfer from Muslim developing world into the core economies by reflecting the subordinate character of financialisation through Islamic finance.

Figure 3.16: Top 10 Countries in Islamic Banking Assets (US$ MN, FYE 2015)



Source: ICD-Thomson Reuters Islamic Finance Development Report (2016)

Based on the articulation so far, and the descriptive study provided in this section, the following section presents an econometric analysis to examine the financialisation and Islamic banking expansion nexus.

3.7.3. Searching for the Sources of Financialisation in Islamic Banking: An Econometric Estimation

This section aims to present the findings based on empirical analysis with the objective of searching for the sources of the observed financialisation caused by the prevailing applications of Islamic finance. In doing so, first, a panel of 14 Muslim-majority countries covering the period of 2002-2014 is constructed to examine the impact of the ascendance of Islamic banking on financialisation trajectory of entire economy to ascertain whether operations of Islamic finance, by and large, strengthen real economy or contribute to further financialisation in economies where domestic market share of Islamic finance reaches medium or high systematic importance.

3.7.3.1. Data, variable definition and model

The selection of sampled countries is based on their market share of Islamic finance in the economy, as evidenced in Figure 3.5. The countries with relatively high percentage of Islamic finance market share is preferred, for it impacts is considered to be more on economic performance. Thus, the list of sampled countries for the econometric analysis in this study is given here with an alphabetical order: Bahrain, Bangladesh, Egypt, Indonesia, Jordan, Kuwait, Malaysia, Pakistan, Palestine, Qatar, Saudi Arabia, Turkey, United Arab Emirates, and Yemen.

Since this study assumes negative implications for Islamic finance on real economic performance, another empirical analysis is conducted under robustness analysis, with a sample of 13 countries covering the period 2003-2014,[34] to examine the impact of the observed financialised economy due to Islamic finance over employment.[35] Sample size in both

[34] Due to data availability issues, we dropped one country (Palestine) and one year (2002) from the panel data when compared to the previous panel data analysis.

[35] Employment is one of the most preferred indicators of real economic performance in both empirical and theoretical studies on financialisation (*see*: Ashman, Mohamed, and Newman 2013; Batt and Appelbaum 2013; Svilokos and Burin 2017 amongst others). In particular, financialisation-employment nexus is stressed by post-Keynesian approach.

empirical analysis is constrained by data availability issue, as data on IBF is highly limited and has only recently been systematised to make it more accessible.

Table 3.5: Definitions and Sources of Variables

Variable	Definition	Source
Financialisation of economy	(i) domestic credit provided by financial sector as a share of GDP (ii) share of finance, insurance and real estate sector (FIRE) in GDP	- World Bank (Word Development Indicators); - Central banks of selected countries; - The Statistical Centre for the Cooperation Council for the Arab Countries of the Gulf ("GCC-Stat"); - Asean Development Bank Statistics; Open Data for Africa Database;
Islamic financialisation	(i) share of financial institutions, banks, real estate and consumer durables (FIRECO) in total financing values of Islamic banks (ii) share of shareholders' equity in total asset values of Islamic banks' (SVO)	Islamic Banks and Financial Institutions Database (IBIS Online)
Trade openness	the sum of exports and imports of goods and services as a share of GDP	World Bank (Word Development Indicators)
Manufacturing	value added in manufacturing as a share of GDP	World Bank (Word Development Indicators)
FDI net outflows	net outflows of investment from the reporting economy to the rest of the world divided by GDP	World Bank (Word Development Indicators)
GDP per capita	logarithm of the gross domestic product per capita	World Bank (Word Development Indicators)
Institutional quality	'rule of law' defined as: the confidence of citizens in law, and the extent that they abide by the rules of the society, such as contract enforcement, property rights, police, and court.	Worldwide Governance Indicators
Unemployment	Unemployment, total (% of total labor force) (modeled ILO estimate)	World Bank (Word Development Indicators)

Considering that there is no academic study exploring financialisation of Islamic finance and its effects on real economy – neither discursive nor empirical, this study takes a pioneering role and constructs its indicators with a meticulous selection to provide an effective reflection of financialisation. Accordingly, definition and data sources for each variable are depicted in Table 3.5, which also lists measures for dependent and explanatory variables and their identification. The rationale for their selection is explained below:

(i) Financialisation of economy: Based on its various definitions and identifications in previous sections, we measure financialisation of an economy with 'domestic credit provided by financial sector as a share of GDP'. Although this indicator is viewed in various World Bank working papers (*see*, for instance, Čihák, Demirgüç-Kunt, Feyen, and Levine 2012) as a measure of financial depth that would pave the way for financial (and then economic) development, we consider it an important sign of financialisation, which leads up to centre finance as an objective function *per se* rather than finance holding an instrumental function for social and economic development. We also employ alternative indicator for financialisation of economy as 'the share of finance, insurance and real estate sector (FIRE) in GDP', which gauges the degree of economy's dependence on financial sector. A list of widely used measures of financialisation in the relevant literature is given before in the Table 3.1. Noticeably, plenty of alternative measures are ready to be used therein, yet the data availability issue constraints us to include in our regression analysis.

(ii) Islamic financialisation: Similar to the rationale for using FIRE sector to GDP in financialisation of economy, we measure Islamic financialisation with 'the share of financial institutions, banks, real estate and consumer durables[36] (FIRECO) in total financing values of Islamic banks.

It can be argued that Islamic finance is an asset-backed financing, and hence deals with trading in goods with holding a real asset in its transactions rather than making profit out of monetary papers only. For this reason, there would not be a case for financialisation in Islamic finance. However, we argue that one of the underlying logics of financialisation is the idea of treating

[36] There can be some controversies on consumer durables and its use as a measure of financialisation, for consumer durables can alternatively be thought contributing to the expansion of aggregate demand and hence contribute to real economy. In fact, most of the consumer durables are provided through consumer credits which strengthen the role of financial markets; as indicated by Lapavitsas's thesis (2011), which argues that workers are involved in the process of financialisation by channelling their wages and salaries into financial system through having micro credits and bank credits for their consumption needs. The argument that consumer credit accelerates financialisation is also iterated by Watkins (2017:110) with his supporting evidences from real world experiences: "… consumer credit, however, accelerated during the period of financialization. The deregulatory movement following the demise of the Bretton Woods Agreement in the 1970s led to rapid innovations in consumer credit and increases in consumer debt". Since it is mainly debt based on the non-existence form of income at the time, consumer credits create fictitiousness through the imbalance in the economy between available monetary means and consumption.

money as a subject matter of trade beyond its role of being a medium of exchange. In this manner, some trading contracts of Islamic finance today operates with this logic to generate huge profits similar to conventional way of profit making. The assets used during the transaction never adds significant value to the real economy since they are symbolically being purchased amongst a pre-determined group of people to generate money without burdening additional risk. This is evident particularly in *bay'ul i'nah*, *tawarruq*, commodity *murabahah* and certain *sukuk* types and issuances.

The experience and the debate in the Islamic finance sphere indicates that a considerable number of Islamic finance practitioners have been trying to find '*Shari'ah* compliant' ways to eliminate the burdens and responsibilities accompanied by adopting an asset-backed Islamic finance. The mentioned contracts above, hence, reflect such an attempt of converging Islamic finance towards conventional financial system. Acknowledging these factors, by using FIRECO as a measure of Islamic finance based financialisation, here, we aim to reveal the degree of concentration on financial and real aspects of economy by Islamic finance.

An alternative indicator of Islamic finance based financialisation is chosen as 'the share of shareholders' equity in total asset values of Islamic banks' (SVO). Based on the post-Keynesian expression of financialisation as shareholder value orientation and also close relationship between shareholder value and employment, we prefer using this indicator as one of the exogenous variables for robustness analysis.

(iii) Trade openness: Measured by 'the sum of exports and imports of goods and services as a share of GDP' and consistent with the prior literature, we consider trade to be an exogenous variable in our regression analysis. Following on the idea of subordinate financialisation conceptualised by Lapavitsas (2013), trade openness is expected to have adverse effect on economic development trajectories of developing countries and hence strengthens the degree of financialisation.

(iv) Manufacturing: We use 'value added in manufacturing as a share of GDP' to examine how productive side of economy impacts financialisation. The debates on pre-mature deindustrialisation (*see*: Cecchetti and Kharroubi 2015; Dasgupta and Singh 2007; Palma 2014; Rodrik 2016 amongst others) suggests that industrialisation process of developing countries was interrupted due to the transition from industrial capitalism towards finance capitalism. Policy makers in such countries have left industrialisation process pre-matured; as, instead, they shifted to concentrate on financial markets and directed investments on this area. Thus,

finance gained utmost importance while neglecting productive fields such as manufacturing and trade. We, therefore, expect that variation in manufacturing sector should have negative effect on financialisation.

(v) FDI net outflows: In order to assess the effect of globalisation on financialisation, Dünhaupt (2014) uses 'FDI outflows as a share of GDP' defined by net outflows of investment from the reporting economy to the rest of the world divided by GDP. This indicator is considered as one of the exogenous variables since it should reckon with the attraction of global financial markets to invest and generate huge profits instead of local investments on home country.

(vi) Log of GDP per capita: This indicator proxies the level of economic development and renders some implications on the change in GDP per capita on the financialisation of economy. It is normally expected that GDP per capita should have adverse effect on financialisation, since an increase on GDP per capita construed as economic prosperity and financialisation is assumed to trigger income inequality. However, high GDP per capita does not directly mean smooth distribution of wealth, thereby it should not be surprising to have positive relationship between these two variables.

(vii) Institutional quality: With an aim of including political economy aspects into the robustness analysis, amongst the very limited alternatives, 'the rule of law' (RoL) is considered as a measure for institutional quality. This is used as part of the effect of non-economic factors on employment in the robustness analysis.

(viii) Unemployment: This variable is considered as dependent variable in the robustness analysis. In doing so, potential contributions of conventional and Islamic banks on macro dimensions of socioeconomic life (employment area in this case) are examined.

Based on the variables defined above, the baseline regression model is expressed in the following form:

$$DOMCRE_{it} = \alpha_0 + \beta FIRECO_{it} + \gamma FIRE_{it} + \delta logGDPpc_{it} + \epsilon TRADE_{it} + \partial MAN_{it} + \tau FDIout_{it} + \varepsilon_{it} \qquad [3.1]$$

where

DOMCRE stands for financialisation of economy;
FIRECO is the proxy for financialisation of Islamic banks;
FIRE is the macroeconomic variable for the degree of sophistication of financial market;

log*GDPpc* is the logarithm of GDP per capita;
TRADE proxies for trade openness;
MAN measures value added in manufacturing as a share of GDP;
FDIout is the foreign direct investment net outflows as a share of GDP;
ε_{it} is the error term;
α_0 is the constant; and
$\beta, \gamma, \delta, \epsilon, \partial, \tau$ are the vectors of coefficient estimates.

In an attempt to explore the impact of Islamic financialisation on real economy and developmentalist trajectories broadly, this study employs a quantitative methodology and makes use of historical statistical data with an unbalanced panel data analysis. A range of econometric techniques are utilised including pooled OLS, random effect and system-GMM estimators to address heterogeneity, over-identification and endogeneity issues. Next subsection provides rationale for applying each of these estimation techniques, their advantages and limitations and also interpretation of regression results in a comprehensive manner.

Before proceeding with the regression results, it should be noted that conducting a panel study on Islamic financialisation poses several challenges. First, unlike discursive approach, empirical evidence requires measurable explanations of Islamic financialisation. In doing so, appropriate indicators should be accessible and available as disclosed information by selected countries. Although there are commonly used indicators for Islamic banking performance, financialisation indicators such as 'value added in finance as a percentage of total value added', 'the size of the financial sector as a percentage of GDP' and 'financial sector's share of profits' are only available for advanced countries. This necessarily leads us to make a careful selection of variables, and hence countries.

Another challenge is related to the difficulty in interpreting developing economies' financialisation trajectory, since it exhibits a subordinate character in Lapavitsas' terms. Despite the nexus of advanced economies and their financialisation process is relatively well-known phenomenon which has been a subject matter of many academic studies in the literature with regularly used variables, financialisation in developing economies have rarely been examined, hence appropriate variables for subordinate financialisation have not been agreed upon.

With an acknowledgement of these challenges, this study should be considered an original attempt in identifying the facets and distinctive features of financialisation of Islamic finance. Not limited with this, it should also be accepted as an authentic attempt since it elucidates developing countries' financialisation trends with an empirical evidence including appropriate indicators.

3.7.3.2. Descriptive statistics and correlation matrix

As part of the initial empirical process, Table 3.6 reports descriptive statistics for 14 countries observed during the period of 2002-2014[37]. The model has medium sample size of 182 observations that can be considered sufficient to reveal reliable results. Amongst the variables used, only 'GDP per capita' is transformed into log values to reduce wide variation across the sample. It is clear that only the indicators of financialisation of economy and trade openness have high variation amongst its values due to relatively big gap between minimum and maximum values.

Table 3.6: Descriptive Statistics (2002-2014)

Variable	Obs.	Mean	Std. Dev.	Min	Max
DOMCRE	182	60.29231	32.79725	-10.15183	143.6417
FIREGDP	182	13.47465	4.805953	6.3692	24.2
FIRECO	182	.4145947	.2334022	0	.9113519
FDIout	182	1.521616	2.651049	-10.35987	9.734888
TRADE	182	88.61905	45.63663	26.85823	210.3738
MAN	182	15.5127	6.184187	4.427057	36.76302
logGDPpc	182	3.80746	.6426834	2.728554	4.861361

Table 3.7: Correlation Matrix

	DOMCRE	FIREGDP	FIRECO	FDIout	TRADE	MAN	logGDPpc
DOMCRE	1.0000						
FIREGDP	0.1678	1.0000					
FIRECO	0.2145	0.4217	1.0000				
FDIout	0.1311	0.1855	0.3285	1.0000			
TRADE	0.4802	0.6389	0.6092	0.3928	1.0000		
MAN	0.3180	-0.2626	-0.2593	-0.1291	0.0605	1.0000	
logGDPpc	0.0634	0.4658	0.5822	0.4245	0.5238	-0.2315	1.0000

Examining the correlation matrix in Table 3.7, the dataset shows that Islamic financialisation has positive correlation with all variables in the model except manufacturing sector. The

[37] The empirical results can be examined as to whether they give biased implications due to the potential outliers used in the dataset. Based on such a consideration, the data is winsorised by removing the potential outliers, and the regression is repeated. However, it is empirically evidenced that the results did not change after winsorisation.

correlation values and signs are almost in line with our expectations since we assume positive relationship between Islamic financialisation and all other variables except manufacturing and GDP per capita. As there is no significantly high correlation amongst variables, the model can be considered trustable in the sense of delivering reliable results.

3.7.3.3. Main results: Pooled OLS, random effect and system-GMM

Table 3.8 depicts the regression results of pooled OLS model, random effect and system-GMM estimators together at a single glance. Before interpreting the results, it should be stated that we do not expect pooled OLS to be an appropriate technique for our panel data model, since it completely ignores country specific effects and does not account for simultaneity bias, instead it pools the entire data in one basket and runs the regression accordingly. Furthermore, this technique violates some basic assumptions including that of error terms. However, with a rationale of rendering comparison with other methods, pooled OLS results shall be interpreted and taken into account with mentioned cautions.

Random effect, on the other hand, reckons with individual specific effects, which is treated to be uncorrelated with explanatory variables. It also assumes no correlation between time-invariant heterogeneity between groups and the error term (Bhargava and Sargan 1983). The choice between fixed and random effect estimation depends on the results of Hausman test, the null hypothesis of which suggests using random effect model. As we ran Hausman test and failed to reject the null hypothesis, and in line with our assumptions over the model, random effect estimation seemed relatively more appropriate technique for our dynamic panel data model. Overall, the model with random effect helps explain 88% of the variability in financialisation values.

Since random effect model does not address endogeneity issues and behaves full exogeneity of the model, system-GMM technique would give much reliable results, for it deals with some essential issues including endogeneity and autocorrelation. This study, accordingly, trusts panel system-GMM estimator[38] developed by Blundell and Bond (1998), which uses both the difference panel data and the data from the original levels specification that eventually enables to produce dramatic increases in both consistency and efficiency. As an alternative to system-GMM estimator, difference-GMM could have been adopted. However, it raises serious problems within its estimation that includes "(i) the elimination of the cross-country

[38] A useful guide for the application of the system-GMM estimator on growth models can be found in Bond, Hoffler and Temple (2001).

relationship and focusing only on time differences, (ii) the suffer from imprecision and potentially biased estimates in small samples, and (iii) exacerbating biases by decreasing the signal-to-noise ratio" (Beck and Levine 2004:432).

Mostly, two main variants of the system panel estimator, one-step and two-step system-GMM, are preferred in econometric studies. While one-step system estimator assumes homoscedastic errors, two-step estimator constructs heteroscedasticity-consistent standard errors, and thus asymptotically accepted to be more efficient relative to the former. Nonetheless, two-step estimator becomes a poor guide for small samples that has large number of instruments, as it raises overfitting problem and may produce standard errors that are biased downwards, which is evident in most of the Monte Carlo experiments. Therefore, one-step system estimator is opted for and robust standard errors are used as common in most studies.

The consistency of system-GMM estimator hinges on the validity of two main assumptions: (i) the error terms do not exhibit serial correlation, and (ii) the instruments must be valid. In addressing these issues, we use two common specification tests suggested by Arellano and Bond (1991), Arellano and Bover (1995), and Blundell and Bond (1998). The first is the Hansen test of over-identifying restrictions, which tests the validity of instruments used in the regression. It should be noted that instead of using Sargan test to address the validity of instruments, Hansen test is applied when robust standard errors are chosen to take place in the regression.

The second test, AR2 test, examines whether the error terms are serially correlated or not. Similarly, Wald test, known as F-test in small samples, examines the joint significance of whether two or more variables should be included in the regression jointly. The p-values of Hansen, AR2 and F test results are given at the bottom of Table 3.8. As the p-values of Hansen and AR2 tests are quite high, 0.843 and 0.454 respectively, we cannot reject the null hypothesis, which means that the model with system-GMM does not pose over-identification and serial correlation issues. F test result, similarly, suggests that the regression model with joint selection of indicators are appropriate.

Following the rationale for each estimation methods explained above, the model presented in Table 3.8 covers the period of 2002-2014 for 14 countries in a cross-sectional manner. As can be seen from the results, the effect and significance of Islamic financialisation on financialisation of economy entirely differs in three estimation techniques. The pooled-OLS and random effect both suggest positive impact, while only the latter is significant at 5%. On the other hand, system-GMM results yield a negative but insignificant effect of Islamic financialisation on dependent variable. It should be noted that, in applying the system-GMM, the variables of FIRE sector to GDP, FDI net outflows, trade openness and manufacturing are treated as endogenous.

These findings are in line with our theoretical premises, for a positive and significant impact in the Model 2 and a negative but insignificant impact in the Model 3 implying that Islamic financialisation either fosters overall financialisation in the sample countries (Model 2) or fails to dilute financialisation trend significantly (Model 3) due to a wide range of reasons including its failure on strengthening real economy. Similarly, system-GMM results invalidate the counter argument that claims Islamic finance to be in no association with financialisation, since it is an asset backed financial proposition that significantly increases trading in goods with real assets, hence giving more weight on real side of economy rather than mere financial sophistication. However, in econometrics terms, the findings cannot clearly imply that the results are robust in terms of rendering same significance and sign. Therefore, the findings must be read within such caveats.

Table 3.8: Pooled OLS, Random Effect, and One-step system-GMM Estimates of Islamic Financialisation on Country Financialisation, 2002–2014

	[1] Pooled_OLS	[2] Random_effect	[3] System_GMM
Islamic financialisation	9.806	16.069**	-0.912
	[0.434]	[0.034]	[0.929]
FIRE sector to GDP	-0.501	1.343**	0.964*
	[0.416]	[0.046]	[0.091]
Log of GDP	-9.556**	-20.810*	-0.367
per capita	[0.026]	[0.054]	[0.938]
Trade	0.405***	0.199***	-0.147*
	[0.000]	[0.001]	[0.069]
Manufacturing	1.277***	-0.586*	-0.555
	[0.001]	[0.070]	[0.571]
FDI	0.135	-1.057**	0.820
net outflows	[0.879]	[0.014]	[0.460]
Constant	43.445***	107.876**	7.379
	[0.008]	[0.012]	[0.810]
Observations	182	182	182
Countries	14	14	14
R-squared/rho	0.340	0.881	-
F_Test/Wald test p-value	0.000	0.000	0.000
Hansen p-value	-	-	0.843
AR2 p-value	-	-	0.454

Notes: *p*-values in brackets; * p<0.1, ** p<0.05, *** p<0.01; The null hypothesis of Hansen test: the instruments used are not correlated with the residuals; The null hypothesis of AR2 test: The null hypothesis is that the errors in the first-difference regression exhibit no second-order serial correlation.

Our theoretical model assumes 'the ratio of FIRE sector in GDP' to deepen financialisation even further since the proliferation of these sectors' share in GDP should lead financial system to move at the centre of economic system. Consistent with this assumption, the variable of FIRE has positive significance over financialisation, with its coefficients 1.343 and 0.964 in random effect and system-GMM respectively. Amongst other macroeconomic variables, per capita GDP, not surprisingly, renders negative effect on financialisation significantly except in the Model 3. Similar to this, manufacturing shows an adverse effect on financialisation basically due to its close relationship with industrialisation that hampers the flourishing of financial investment at the expense of real economic investment.

The impact of globalisation, identified with 'FDI outflows as a share of GDP', on financialisation is ambiguous once looking at three different models. While random effect results suggest that globalisation decreases the degree of financialisation, as FDI outflows target not global financial sectors but rather catch real investment opportunities, findings from system-GMM, contrarily, treats globalisation to be worsening factor for financialisation. Both interpretations make sense, since the real effect of globalisation on developing countries' economic performance has not still been unanimously identified.

Having strong affinities with globalisation, trade openness is located under the general theme of subordinate financialisation, and hence expected to stimulate financialisation. The findings in the first two models yield support to this idea with positive significance at 1%, yet the sign of the coefficient turns out to be negative in system-GMM, meaning that open trade paves the way for increasing real economic activities globally instead of facilitating the reach of global financial operations through financialisation.

3.7.3.4. Robustness analysis

In this subsection, robustness check is applied to examine whether the results are robust to alterations in the conditioning information set and also to changes in the measure of financialisation of Islamic banks. The model aims to examine the impact of financialisation (both Islamic and conventional finance) on unemployment, which is accepted to reflect an important socioeconomic dimension. As mentioned before, the sample consists of 13 countries and covers the period 2003-2014, as data unavailability further limits us with the addition of new variable of unemployment.

We use following model for robustness analysis:

$$UNEMP_{it} = \alpha_0 + \beta SVO_{it} + \gamma FIRE_{it} + \delta logGDPpc_{it} + \epsilon TRADE_{it} + \partial MAN_{it} + \tau FDIout_{it} + \theta RoL_{it} + \varepsilon_{it} \quad [3.2]$$

where

UNEMP denotes unemployment;
SVO is the proxy for Islamic financialisation;
FIRE represents financialisation of economy;
log*GDPpc* is the logarithm of gross domestic product per capita;
TRADE proxies for trade openness;
MAN measures value added in manufacturing as a share of GDP;
FDIout is the foreign direct investment net outflows as a share of GDP;
RoL is the proxy for institutional quality;
ε_{it} is the error term;
α_0 is the constant; and β, γ, δ, ϵ, ∂, τ, θ are the vectors of coefficient estimates.

Table 3.9: Pooled OLS, Random Effect, and One-step System-GMM Estimates of Financialisation on Unemployment, 2003–2014

	[1] Pooled_OLS	[2] Random_effect	[3] System_GMM
Islamic financialisation	-17.371*** [0.001]	2.277 [0.305]	-0.711 [0.912]
Country financialisation	0.155* [0.096]	-0.083 [0.157]	-0.034 [0.742]
Log of GDP per capita	-3.487*** [0.000]	-6.030*** [0.000]	-2.389** [0.041]
Trade	-0.004 [0.661]	-0.006 [0.257]	0.007 [0.394]
Manufacturing	-0.055 [0.363]	0.150*** [0.000]	-0.174* [0.081]
FDI net outflows	-0.332** [0.011]	0.046 [0.213]	-0.134 [0.272]
Rule of law	0.005 [0.764]	-0.035** [0.035]	0.020 [0.412]
Constant	21.598*** [0.000]	30.297*** [0.000]	13.429** [0.015]
Observations	156	156	156
Countries	13	13	13
R-squared/rho	0.447	0.956	-
F_Test/Wald test p-value	0.000	0.000	0.000
Hansen p-value	-	-	0.523
AR2 p-value	-	-	0.746

Notes: (i) *p*-values in brackets; * p<0.1, ** p<0.05, *** p<0.01; (ii) the null hypothesis of Hansen test: the instruments used are not correlated with the residuals; (iii) The null hypothesis of AR2 test: The null hypothesis is that the errors in the first-difference regression exhibit no second-order serial correlation.

Presenting the results of robustness check, Table 3.9 depicts a similar view and categorisation of estimation techniques with Table 3.8. Leaving pooled-OLS results aside because of the reasons explained before, random effect results show that both Islamic and conventional financialisation does not exhibit significant impact on unemployment. This might be due to the pre-mature nature of financial system in developing economies, which have not penetrated into the entire economic system yet; hence, it is unable to influence employment significantly. Other variables such as institutional quality (RoL) and GDP per capita, not surprisingly, reveal negative effect on unemployment.

The results of system-GMM renders negative but insignificant effects of Islamic and conventional financialisation on unemployment, which can help to suggest that subordinate financialisation in developing countries, contrary to the role of financialisation in advanced economies, does not hold a significant influential role yet on macroeconomic indicators, such as unemployment.

3.8. CONCLUSION

Islamic finance and financialisation phenomenon have barely been associated in the literature of Islamic economics due mainly to ignorance, or at best, an unwitting negligence of the term by practitioners and theoreticians. Despite the introduction of 'financialisation of Islamic finance' presumably sparks off a perplexing situation in such an environment, it is worth to shed light on the failure of Islamic finance project from the perspective of financialisation since the failure roots in, to a large extent, the adopted financial logic borrowed from mainstream economics whereby the utmost importance is given to financial sector to take place and substantialise at the core of economic activities.

In the meantime, the scope of failure is controversially multifaceted, while this study identifies it with the Polanyian notion of embeddedness. Accordingly, the participatory and sharing-based values embedded in the Islamic financial contracts throughout the ages has faded away in the modern times by giving way to efficiency oriented and market driven understanding of Islamic finance, which cherishes shareholder value maximisation in its operations and favours more on debt-based financial instruments as part of capitalism based institutional logic that are both observed in the empirical analysis in this study. Thus, the practical applications of Islamic banking subordinated Islamic economic theory in the service of converging towards conventional financial system, which, in return, created a disembedded feature of Islamic financial industry. While in an aspirational sense, Islamic banking is considered as a disruptive financing force, the emergence of financialisation of Islamic banking should, accordingly, be understood as an attempt of disembedding shared norms, values and beliefs from economic realm that eventually leads up to create a self-regulated and standalone industry of Islamic finance. As in the case of financialisation in advanced economies where financial markets dominate entire economic system with the pursuit of generating profit at the expense of engendering social inequality and distributional problems, financialisation of Islamic finance, far from conceiving developmentalist outcomes, helps create a financialised commercial society within Muslim domain. The disenchantment with Islamic finance is, hence, pertain to such a process of disembeddedness, which therefore has led to the emergence of '*Shari'ah* compliant vs Islam based' financing debate.

Ideally speaking, Islamic finance should have emerged as a bottom-up demand from society to meet financial needs of individuals under a simple but functional role of 'financing' *vis-à-vis* a self-proclaimed 'finance' understanding constructed by mainstream economics. Nevertheless, Islamic finance could not position itself with a moral economy understanding and has always targeted to shine out as an alternative market segment within global financial system. The gradual process of diverging from moral economy perspective is elucidated through historical facts and conditions of Muslim world surrounded by a new regulation of world financial system in the post-war period.

In a general sense, discursive aspect of Islamic financialisation is located throughout the study, to constitute the theoretical ground, with a moral economy understanding under the rubric of Polanyian embeddedness debate. In addition, the general idea of financialisation of Islamic finance is supported with the evidence provided through empirical analyses, which demonstrates that Islamic finance exacerbates financialisation process of economy in which it has some level of presence, or, as other estimation technique suggests, it fails to bolster real economy by lessening the degree of financialisation. It implies, therefore, that Islamic financial area, not different than the conventional design, failed to evade the dominance of capital fundamentalism and lost its position as an instrument to contribute to social good rather than as an end itself. Even worse, Islamic banking seems to be serving the proliferation of capital by creating tension with other stakeholders such as labour, land and money. In other words, the evidence suggests that financial process can be maintained for the accumulation of capital and profit maximisation of those who maintain capital-intensive investment activities through fictitious commodities.

While the explanation of historical and hegemonic social formational factors clarifies the rationale for the convergence of Islamic finance towards financialisation, the scope and dimensions of the convergence are further crystallised in light of different views on financialisation categorised under six approaches as discussed in the initial section above. Accordingly, the theoretical debate and empirical evidence on financialisation of Islamic finance, developed throughout the chapter, unravelled broad affinities with each approach and their main emphasis on and features of financialisation. Firstly, the failure of Islamic banking operations in promoting real economy confirms the post-Keynesian emphasis on slowdown of real economic activities due to the ascendance of financial sector. In addition, in examining short-run and long-run orientation of financial activities in the post-Keynesian approach, the figures on the distribution of the modes of Islamic finance above ensure that the logic of generating profits through short-termist contracts dominates and permeates through Islamic banking sector, as evident in the small share of long-run project financing contracts such as *mudarabah* and *musharakah* based project financing. The empirical evidence produced by this study confirms the Marxian and varieties of capitalism approach, too, in the sense that the expansion of Islamic finance in all over the world seem to create an accumulation crisis through shareholder value orientation in the near future, since the capital accumulation within Islamic banking cannot expand into different categories of society, as participation, profit and loss as well as risk sharing features are very limitedly applied in different Islamic contracts. Furthermore, the implications of the observed and evidenced financialisation of Islamic finance influence everyday life of Muslims similar to cultural economy approach, such that the expansion of the prevailing understanding of Islamic banking encourages to construct a new form of debt-based society, albeit motivated by religious concern. In other words, financing no longer become an ordinary instrument to fulfil everyday necessities, but it leads to create, under Islamic finance, a temptation to continuously search for financial ways to sustain individual and social life.

The results, in a nutshell, show that developmentalism as a social objective could not be revealed due to heavy financialisation of Islamic finance. What leads it to such a situation called 'social failure' is highly related to methodological obscurity in defining the objectives of Islamic economics. Objectivist and teleological perspective on Islamic economics and finance necessitates a moral economy understanding, which is extensively scrutinised in this chapter. Islamic finance, in this sense, should settle its instrumental role of 'financing' as an objective to help creating an economic system based on Islamic principles. However, it went the other way around and created further disembeddness. In this regard, Islamic financialisation denotes one of the reflections of social formation of contemporary Muslim societies through which economy gains an autonomous sphere from other social layers by disembedding widely shared values, norms, and other non-economic factors from the economic realm. It also creates commodifying social relations that no longer embraces its traditional role of reciprocity, but rather replaces with transactions under the whole objective of efficiency some of which are fictitious as the practice of organised *tawarruq* demonstrates. In this sense, commodifying social relations removes the reciprocity between individuals, and relegates economic interactions between individuals to transactional level. For instance, there can be no objections towards organisational *tawarruq* while looking at transactional perspective; however, its legitimacy should be criticised when the reciprocal consequences are considered. Thus, commodifying social relations is necessarily an outcome of relegating everything into transactional level without reckoning with individual and social implications. This brings us Oscar Wilde's famous quote in summarising the debate: "Nowadays people know the price of everything and the value of nothing" (Wild 2015).

CHAPTER 4

RE-EMBEDDING *MAQASID AL-SHARI'AH* IN THE ESSENTIAL METHODOLOGY OF ISLAMIC ECONOMICS

4.1. INTRODUCTION

The idea of Islamic economics burgeoned as a post-colonial counter-hegemonic attempt to address the observed developmentalist failures of Muslim societies in a period where old colonial legacies had remained overwhelmingly shaping socioeconomic institutions in decolonized Muslim lands. Since the prevailing legacies are considered to impede emancipation and empowerment of Muslim identity, obliterating their traces was seen an essential concern in developing an authentic meaning of economy and society as part of identity search. Islamic economics, thus, emerged as a project to develop an Islamic system of economics based on Islamic normative principles and substantive morality.

This project has aimed at coming to terms with the challenges Muslim individuals and societies facing with the mainstream materialistic understanding of the economy in such a way to rescue the meaning and function of human agency, land, labor and capital as well as the extended stakeholders in the Islamic social formation to generate a participatory and sharing economy. Consequently, considering the ideational mismatches between Islamic and secular worldviews, Islamic economics envisaged to function in eliminating the dependence upon capitalist formation of economic life and help to construct a new social formation of Muslim societies in the light of Islamic ontology and epistemology. In achieving this, in the short-run, utmost importance is given to public policy oriented developmentalist agenda with the objective of eliminating underdevelopment, eradicating poverty and weak politico-economic structures, while in the long-run an attempt is considered in developing Islamic social formation.

The theoretically defined aspirations of Islamic economics are invariably welcomed and encouraged to put into practice, yet the historical experience has shown that the institutionalisation process has been limited to banking and financial activities with an unsophisticated and non-theoretical making of Islamic finance. General trend of Islamic economic studies has, thus, been moving towards finance and bank centred view of Islamic economics in which financial operations constitute the pivot of economic activities.

As the developmentalist aspirations were hedged around Islamic financial sphere, the performance of Islamic banks and non-bank financial institutions in regard to their contribution to social and economic development became more significant. Thus, the emergent phenomenon of Islamic finance and its nexus with developmentalism is examined by considering its moral articulations and outcomes through essentialising value-based mode of financing. In line with this, it was evidenced empirically in Chapter 2 in this research that Islamic banks failed to establish a development-centred view of financial activity envisaged in theory of Islamic moral economy (IME), but they have rather opted for strategies of homogenisation in global financial system as an alternative market segment operating not differently from conventional finance understanding by replicating the prevailing frame. This is considered as divergence from ideals to the mimicry of conventional finance through representing hybrid financial services (Asutay 2007b, 2012).

After the recognition that the divergence of Islamic finance culminates in mimicry and hybridity, it is worth to shed light on the failure of Islamic finance project from the perspective of ‘financialisation’ since the failure roots in, to a large extent, the adopted financial logic borrowed from mainstream economics whereby the utmost importance is given to financial sector to take place and substantialise at the core of economic activities. This approach necessarily raises the notion of ‘financialisation of Islamic finance’ and its discursive power to explain the rationale behind the failure of social performance of Islamic banks. The emergence of financialisation of Islamic finance should, accordingly, be understood as the attempt of disembedding shared norms, values and beliefs from economic and financing realm that eventually leads up to create a self-regulated and standalone sector of Islamic finance.

As in the case of financialisation in advanced economies where financial markets dominate entire economic system with the pursuit of generating profit at the expense of engendering social inequality and distributional problems, financialisation of Islamic finance, far from conceiving developmentalist outcomes, sparks off a sort of financialised commercial society within Muslim domain. The disenchantment with Islamic finance, hence, pertains to such a process of disembeddedness. Financialisation of Islamic finance, therefore, denotes one of the reflections of social formation of contemporary Muslim societies through which economy gains an autonomous sphere from other social layers by commodifying social relations that no longer embraces its traditional role of transforming the society through moral economy objectives such as reciprocity and participatory economy, but rather is replaced by transactional paradigm under the neoclassical objective of efficiency. The empirical analysis in Chapter 3, in parallel with this assertion, evidenced that Islamic finance exacerbates financialisation process of economy, or, similarly, it fails to bolster real economy by lessening the degree of financialisation.

While non-developmentalism and financialisation together help develop a strong argument in explaining the rationale behind the social failure of Islamic finance, they can be considered as the articulations of methodological obscurity in defining the objectives of Islamic economics. In this manner, both the developmentalist failure of Islamic finance and the financialisation process ascertain that the initial concern with theory making should be on methodological issues, for knowledge can only be authenticated through a rigorous methodology. This essay, therefore, turns the focus on methodological issues by opening a discussion on *maqasid al-Shari'ah,* which constitutes the fundamental base in Islamic finance related methodology.

4.1.1. Problem Statement

Methodological approaches within Islamic economics has scarcely been debated in academic studies and it has brought to the surface two opposing views on the right methodology to be followed in theory building of Islamic economics. The first view grounds its basic argument on the idea of 'Islamization of knowledge' (IOK) devised by al-Faruqi (1921-1986). Although Faruqi's IOK paradigm is highly sophisticated and hence deserves careful evaluation for its articulation, in their *fiqhi* and modern construct of Islamic finance, most Islamic finance experts have made pragmatic references to the IOK paradigm in their attempt to replicate conventional financial practices in disguise of 'Islamization' process by locating Islam as pre-fixes or 'form' but not necessarily in 'substance'. Thus, IOK was simplified in the hands of Islamic finance practitioners, academics and *Shari'ah* scholars as a method, and it has been instrumentalised to espouse mainstream and Islamic understanding of finance with eschewing philosophical contributions of al-Faruqi.

The second view suggests having recourse to the original scripts and reinterpret them in order to fathom out ontologically authenticated and epistemologically substantiated Islamic paradigm of economic system. The practitioners of the former approach mostly applied *fiqhi* or juridical methods including tricks (*al-hiyal al-fiqhiyyah*) in justifying controversial issues and legitimatising applications within Islamic finance sector, which was seen and hence criticised by many including Ibn al-Qayyim (1292-1350) many centuries ago. The proponents of the latter approach, on the other hand, have harshly criticised the Islamization process within Islamic finance and stipulated a bottom-up and ontologically referenced authentic reconstruction of economic institutions by rejecting Western economic models as reference.

Interestingly enough, both trends have been involved in a revived discourse on *maqasid al-Shari'ah* in supporting their arguments, which is interpreted as the higher objectives and intents of Islamic law implying that every action should be conducted by leading to human well-being. For instance, it is widely advocated by some *Shari'ah* scholars in the first view that Islamic finance should be seen as a market driven sector. Thus, potential disputes on *Shari'ah* compliancy during the interaction between Islamic financial operations and conventional market design can be resolved in the light of *maslahah* (public interest) and *maqasid.*[39] This expedites the process of integrating Islamic finance into the global financial system resulting into Muslim societies prospering and developing.

On the contrary, critiques of this approach reject such an understanding of *maqasid*, which is believed to blur the content of the term and pave the way for embracing toxic products and practices in the name of *maslahah* in the simple meaning that 'there is a public interest in such transactions'. Instead, they suggest using *maqasid al-Shari'ah* as a particular framework, which is mainly located in the theoretical expression of al-Ghazalian understanding, to identify and articulate developmentalism[40] with the objective of *Shari'ah*. Grounded on such endeavour, various *maqasid* indices based on the Ghazalian five necessities[41] were developed to evaluate performances of Islamic banks and economies in general. In doing so, *maqasid* is identified and interlinked with some popular concepts including corporate social responsibility (CSR), corporate governance (CG), environmental, social and governance (ESG), sustainable development goals (SDGs), and human development (HDI). Furthermore, these concepts were appropriated and transferred into Islamic economics literature to show that *maqasid* already incorporates them all; thereby these initiatives represent only one aspect of *Shari'ah* objectives. In line with this, empirical studies on the nexus of *maqasid* and Islamic finance started to

[39] Typical examples are evident in the legitimization of highly controversial Islamic financial instruments such as *tawarruq*, *bay'al-'inah* and specific *sukuk* applications.

[40] This study recognizes the value-loaded definition of 'developmentalism'. However, it also recognizes that Islamic aim is not only economic development but multi-faceted development within the parameters of *adalah, ihsan, rububiyah and tazkiyah* in the context of *tawhidi* paradigm (Asutay 2013). Hence, developmentalism is redefined within Islamic normativeness by essentialising human-centered development by re-defining individual as Islamic economics "aims at the study of human falah achieved by organizing the resources of earth on the basis of cooperation and participation" (Khan 1984:54). In this context, re-defined developmentalism is objected towards emancipation and empowerment in every aspect of life within the *ihsani* social formation.

[41] These consist in the preservation of faith, self, intellect, posterity, and wealth. Al-Ghazali was the first to enumerate them as making up the category of universal necessary (*daruri*) *maslahah* whose safeguarding is intended by the Divine Law (*shar'*) and which constitute the foundation of human society (*see*: Ghazali 1997: 417).

proliferate through following the popularisation of abovementioned concepts under *maqasid* terminology.

As can be seen, theoreticians and practitioners on both sides tend to make use of *maqasid* merely as a 'floating signifier'[42], since the term is wittingly used for absorbing desired meanings into the concept of *maqasid*. At best, thus, *maqasid al-Shari'ah* has been assigned the task of bestowing legitimacy in an instrumental manner for *Shari'ah*-compliant products and practices in a formalistic way. Developmentalism, on the other hand, could not be reformulated with *maqasid al-Shari'ah* perspective in neither way, albeit the latter approach claims to reach it through developing some *maqasid* indices. Thus, what happens at the end is a pragmatic, instrumental and eclectic use of *maqasid* that eventually has led to the malaise of Islamic banking and finance (henceforth; IBF) and diminished the close link between developmentalism and *maqasid al-Shari'ah* for the sake of yielding efficiency in the practices of IBF. Due to such a failure, the current practice of Islamic finance has to be considered as the 'second best solution' (Asutay 2012:109) in relation to developmentalist objectives.

4.1.2. Aims, Objectives and Research Questions

This study argues that the social failure of Islamic finance in relations to realising developmentalist outcomes and its negations of moral expectations is highly a methodological problem, not just an issue bounded with practical realities of the field. Therefore, this research aims to suggest *maqasid al-Shari'ah* as the fundamental knowledge creation methodology for the theorisation of Islamic economics through which Islamic developmentalism conceptualised and transformed into public policy making. However, it criticises market-oriented understanding and practice of *maqasid*, which is extensively applied in Islamic finance as an instrumentalization of morality and legitimacy gaining tool leading up to a new moral code of conduct for economic activities. In responding to this, this study aims to develop an authentic approach towards *maqasid al-Shari'ah* based on substantive morality that shapes the behaviour in an embedded manner, and proactivity in the sense of dynamic application to the realm of economics and finance.

Beyond instrumental and eclectic approaches, this study argues that the theoretical grounds of Islamic economics should be re-examined in light of the proactive and substantive morality articulated *maqasid al-Shari'ah* framework with its nine dimensions, beyond the traditional Ghazalian *maqasid*, as elaborated later. By doing so, the rationale behind the failure of realising

[42] According to the Oxford Reference dictionary, the term means: "A signifier without a specific signified. Also known as an 'empty signifier', it is a signifier that absorbs rather than emits meaning." For the historical use of the concept, see: Mehlman (1972).

Islamic developmentalism in post-colonial Muslim nations can better be explained, since proactive *maqasid* envisages an effective methodology in articulating moral consequences of economics and finance, and, consequently, suggests a different approach towards developmentalist considerations when compared to existing applications of *maqasid* based on methodological individualism.

Based on these aims, the following objectives are developed:

(i) to conduct a critical review of the *maqasid al-Shari'ah* from historical contenders to the contemporary applications;

(ii) to present a critical review of *maqasid al-Shari'ah* related empirical studies;

(iii) to identify the shortcomings of the existing frame and application of *maqasid al-Shari'ah*;

(iv) to propose a new understanding and constituting a practice of *maqasid al-Shari'ah* through re-embedding Islamic morality to produce development consequences.

In accordance with the identified aims and objectives, this study raises the following research questions:

RQ_1: How should *maqasid* be designed in order to deliver an authentic and functional methodology for Islamic economics?

RQ_2: In what sense the prevailing *maqasid* perspective in Islamic finance diverges from the aspirations of Islamic economics?

RQ_3: What are the consequences of the prevailing Ghazalian *maqasid* framework in relation to Islamic moral economy expectations?

RQ_4: What is the nature and constituents of an effective *maqasid* to embed Islamic morality in definition and operations of Islamic economics and finance?

The following section aims, initially, to provide a foundational ground for the concept of *maqasid al-Shari'ah* through dissecting its historical evolution with special contributions by Islamic scholars. After that, *maqasid* is contextualised within the theoretical aspects of Islamic economics and practical field of Islamic finance.

The rest of the chapter is organised as follows: Section 4.2 presents conceptual and historical perspective in *maqasid al-Shari'ah* as well as its evolution throughout the centuries within Muslim intellectual domain, while Section 4.3 discusses the approaches towards *maqasid* and its classification. Section 4 delves into the theoretical association between *maqasid* and Islamic developmentalism whereby particular attention is given to the literature of Islamic economics and *maqasid* nexus. Section 5, lastly, elaborates on the nature, dimensions and functionality of constructing a proactive *maqasid*-based development model that envisages re-embedding *maqasid* into the theory making of Islamic economics.

4.2. *MAQASID AL-SHARI'AH*: A CONCEPTUAL AND HISTORICAL PERSPECTIVE

Based on the fundamental principle that every act in practice or idea in mind emanates to actualise certain intention or objective in the real life; *maqasid al-Shari'ah*, in a similar vein, aims to discern what Allah commands, through His revelations, to achieve in this world and in the hereafter by the hands of human beings and other creatures. Once this is ascertained, the whole idea of banking and finance is then canalised into the fulfilment of this objective. In the case of IBF, *maqasid al-Shari'ah* is believed to formulate entire functioning of Islamic modes of finance so that it should serve human wellbeing and ensure social welfare through an extended stake-holding paradigm due to the *tawhid* axiom. Practical applications of IBF would, then, be examined with reference to the *maqasid al-Shari'ah*. Thus, it is crucial to identify *maqasid al-Shari'ah* and its theoretical and philosophical foundations and practical implications under the developmentalism subject, as the articulation of *maqasid* in a consequentialist manner refers to developmentalist objectives.

4.2.1. *Maqasid al-Shari'ah*: A Conceptual Exploration

Although it is all agreed that 'Islamicity' of IBF is recognized by its compliance to the Islamic law, very few people discuss as to what constitutes the Islamic law. Is it referred to *fiqh*, *Shari'ah, qanun* or something else with the Islamic law? This question has tremendous importance in the sense of making a pure distinction between *fiqh* and *Shari'ah*, which allows us to go beyond confining ourselves to what Muslim scholars understand from the scriptural texts while searching for their purposes. Fundamentally, *fiqh* is the "knowledge of practical revealed rulings extracted from detailed evidence", hence it "represents the 'cognitive' part of the Islamic Law … while *Shari'ah*, by definition, represents the 'heavenly' part of this law" (Auda 2007:57). It is due to this reason that *faqih* is used for human beings dealing with *fiqh* and *al-Shari'* is for Allah. Consequently, *fiqh* must be acknowledged as the reflection of human cognition (*idraq*) aspect of the revealed knowledge. In this respect, *maqasid al-Shari'ah* must be defined as the higher objectives of the revealed way of life, rather than the higher objectives of what *fuqaha*[43] deducing it from *Qur'an* and *Sunnah*. In the IBF context, this definition helps us to uncover the crux of finance related controversies in the Islamic law.

[43] It is the plural of, *faqih,* who is a scholar of Islamic jurisprudence.

After clarifying the contrast between *fiqh* and *Shari'ah*, now *maqasid* and its theorisation should be incorporated into the analysis. Literally, the term *maqasid,* singular *maqsid,* connotes the meaning of objectives, ends, purposes, intents or goals. When *Shari'ah* is attributed to *maqasid* in the compound form *maqasid al-Shari'ah*, it refers to the wisdom and purposes underlying the Divine commands as being intended for the good and well-being of human beings as well as other creatures (Ibn Ashur 2006). As discussed in this chapter, *maqasid al-Shari'ah* have far-reaching implications in respect of Islamic banking and finance.

Ibn Ashur, one of the contemporary Islamic scholars that contributed much to the theory of *maqasid*, emphasises the substantial function of *maqasid* as "the fact that it answers to inborn human nature (al-*fitrah*)" (taken from Attia 2007:11). This implies that Ibn Ashurian conceptualisation of *maqasid* is attributed to the concept of *fitrah* as the ground for *maqasid*. The scope of *maqasid al-Shari'ah* is, then, formulated by al-Shatibi through an inductive method. In his view, induction constitutes the principal method in derivation and identification of *maqasid* (Raysuni 2011:282). Similarly, Ibn Ashur stipulated some conditions for the legitimacy of *maqasid* through assigning certain characteristics to it: "(a) *thubut*: that is to say, they must be based on texts which have been narrated and passed down in a reliable manner; (b) *zuhur, i.e.*, implying that they must bear a meaning which is clear and self-evident; (c) *indibat;* that is, they must be consistent from one person, place, time and circumstance to the next; and (d) *ittirad* that is, they must be consistent, and regular" (taken from Attia 2007:12).

Due to the extent of the scope and comprehensiveness of *maqasid*, some other concepts have been interchanged with *maqasid* in identifying a particular phenomenon. This conceptual resemblance between *maqasid* and other concepts (such as *illah* and *maslahah*), especially for the controversial issues in Islamic law, leads to some perplexities amongst contemporary Islamic scholars such that the investigation of *maqasid* for certain rulings, in the *Qur'an* or in historical evidences, becomes difficult owing to mixing up *maqasid* with other terms as discussed below. Reflection of this problem in the Islamic economics and finance field implies that developmentalist objectives of societies are wrongly identified and applied over its institutions.

Since the differentiation of these concepts from *maqasid* does play a vital role on the construction of *maqasid* theory, some of such fundamental concepts are briefly alluded here. One of them is the concept of *maslahah*, which basically means 'public interest'. While some of the early legal theorists like al-Juwayni (1028-1085), especially in the period when *maqasid* was not thought to be a standalone discipline, used these two terms interchangeably, some others including al-Ghazali differentiated both terms by placing *maqasid* under *maslahah* domain. A more favourable explanation was rendered by al-Tufi (1259-1316), who defined *maslahah* as "what fulfils the purpose of the Legislator" (taken from Auda 2007:2). On the same line, the validity of *maqasid* is stipulated by al-Qarafi (1228-1285) such that *maqasid* has to reveal some benefit (*maslahah*) or avoid some harm (*mafsada*) in the individual and societal level. It is concluded with these two approaches, that *maslahah* should be seen as the entire process of realising, or the ways which fulfil, that *maqasid*. This implies that *maqasid* provides the framework in which *maslahah* should be located.

Another important misconception stems from the understanding that highlights causes or '*illah*', over *maqasid* while searching for objectives of scriptural rulings. A famous narration about one of *Khalifah* Umar's *ijtihads* or independent reasoning can be a good example to crystalize the issue. According to the narration, Umar made an *ijtihad* of disapplying *Qur'anic* punishment for cases of theft that occurred in the period when Muslims were suffering from a devastating famine. The *illah*-based interpretation of Umar's *ijtihad* necessitates that if those who are in need during the famine times engage in theft, the *Qur'anic* punishment should not be applied. When it is misunderstood by ascribing that Umar made this *ijtihad* just by considering the cause for theft, then his *maqasidi* perspective would be easily overlooked. His *ijtihad*, then, benefits for contemporary Muslim *Ummah* once exclusively the same *illah* comes into existence again. However, his *maqasidi* interpretation goes beyond the mere concentration of *illah* for a specific ruling, which is already subject to change in every circumstance, and renders a more extensive and persistent approach within which wisdoms and objectives that are applicable in all times can be deduced from that ruling. By the same token, challenges in IBF, which are impossible to be tackled through an *illah*-based approach can be dealt with a sound *maqasidi* way.

The causation-based way of thinking in Islamic law, in fact, hinders the flourishing dynamicity, creativity and flexibility of Islamic philosophy, and also the potential of benefiting from historical evidences in dealing with current problems, especially in IBF. In other words, the dynamic nature of Islamic law has been made dysfunctional by the shift of *maqasid*-based approach towards causation based one through the adoption of the view that we cannot think of an action without its causes rather than without its purposes. Similarly, every action is explained in terms of cause and effect interaction. This approach is quite reminiscent to the disengagement process of Western thought from teleology to causation since the birth of Western science predicated its ontology to the adoption of causality paradigm. In short, a holistic and purpose-oriented understanding is essential in order to evolve causation into holism and expand *maqasid* into the core of contemporary Islamic jurisprudence.

4.2.2. Ontological Approaches and Historical Contributions towards *Maqasid al-Shari'ah*

The basic motivation for getting involved in the *maqasid al-Shari'ah* stems from the fact that Muslims seek to know wisdom, bases or purposes of the Islamic rulings through which they would able to uphold an Islamic way of life. This overarching nature of *maqasid* paved the way for it to be a widely appealed method that is utilised at any time in the history, from the first Prophetic times to the postmodern era, namely the current times. However, the study of *maqasid* as a theoretical discourse under certain subjects or disciplines, and its theorisation can be traced back to the first Islamic centuries after the Prophet Muhammad's Companions' era including the followers of the Companions (*tabeen*).

While *maqasid* issues were dealt in the Companions' era in a practical way through consulting with the Prophet, it was first used as a concept in the works of Al-Tirmidhi (820-869), al-Qummi (918-991) and others during the first three Islamic centuries. Systematic studies on the theory of *maqasid*, however, were believed to start with al-Juwayni. Despite the fact that *maqasid* was considered to be a subject under *usul al-fiqh* or methodology of *fiqh* in a traditional manner, it was by the 5th century onwards, with the great contributions of al-Ghazali and al-Shatibi, that *maqasid* as a substantial methodology for *usul al-fiqh* was emerged (Auda 2007:xxv; Kamali 2008:9). This section hence aims to present the contribution of the contenders in the development trajectory of the *maqasid* knowledge and methodology.

4.2.2.1. Abu al-Ma'ali al-Juwayni (d. 478/1085)

Juwayni is the first Islamic jurist who pioneered the systematisation of *maqasid* theory by introducing five levels of *maqasid*. In his novel attempt, he did not only identified the levels as "[essentials] (*darurat*), public needs (*al-hajah al-'amah*), moral behaviour (*al-makrumat*), recommendations (*al-mandubat*), and 'what cannot be attributed to a specific reason'" (Auda 2007:17), but also formulated the principal essentials as the preservation of (i) faith, (ii) human life, (iii) faculty of reason, (iv) progeny, and (v) material wealth'. His five levels of *maqasid* was, then, reduced to three levels of necessities, 'essentials (*daruriyyat*), exigencies (*hajiyyat*), and embellishments (*tahsiniyyat*)', due to his conclusion that the third and fourth levels can be combined into one, and the last level does not fit none of the three levels (Kamali 2008:10; Raysuni 2011:15).

With the embedment of levels of necessity into the *maqasid* theory, his successors and disciples are indebted to him for his contributions, and thanks to these contributions, Juwayni has hitherto been commemorated.

4.2.2.2. Abu Hamid al-Ghazali (d.505/1111)

Al-Ghazali, a disciple of al-Juwayni, developed the theory of *maqasid* in such a way that his descendants have availed themselves of his contributions significantly. His ideas were influenced and shaped, with a great degree, by Greek logic, albeit he generally rejected Greek philosophy for its pagan character.[44] In particular, al-Ghazali adopted Aristo's 'logical tool' to use as a methodology for the derivation of knowledge and concluded that the logical tool should be treated as the starting point for all 'branches of knowledge'. In doing so, he "internalised Greek logic as a way of thinking" (Auda 2007:208), and, for this reason, he was exposed to critics raised by al-Taymiyyah and other scholars. Putting these critics aside for now, one of the most significant contributions of al-Ghazali to the theory of *maqasid* would be the introduction of 'syllogistic deduction' as a method for the methodology of analogical reasoning (Auda 2007:208).

As al-Ghazali did not consider *maqasid* as a standalone discipline, he located it under the concept of *maslahah*. His definition of *maslahah* basically refers to any 'interest' that leads to the achievement of benefit and prevention of harm (Al-Ghazali 1997). Therefore, the principal function of *maslahah* is the preservation of objectives of Islamic law, in other words, preservation of *maqasid al-Shari'ah* (Attia 2007:97). Here, Ghazalian *maslahah* dissociates itself from *maqasid*, in terms of functionality, through undertaking the role of preservation in realising *maqasid*.

An important feature of the theoretical frame of Ghazalian *maqasid* is that it embodies a holistic approach, which does not allow assigning single causes for Islamic rulings, and which necessitates multiple evidences from *Qur'an*, *Sunnah* and other secondary sources to reckon *maqasid* as legitimate (*see*: Attia 2007:115; Auda 2007:217). However, beyond these, al-Ghazali is mainly remembered with his contribution of ordering the essentials as (i) *al-Din* (faith), (ii) *al-Nafs* (human life), (iii) *al-'Aql* (faculty of reason), (iv) *al-Nasl* (progeny), and (v) *al-Mal* (material wealth).

It is important also to note that al-Ghazali never limited the essentials into a particular bundle of numbers, rather he laid stress on the most important ones among them. At first, he categorised objectives of Islamic law, in his first book *Shifa' al-Ghalil*, under *maqasid* of worldly interests and that of religious affairs. After recognising the serious problems of creating this duality, later

[44] For further discussion on Ghazali and his ideas interacting with Greek philosophy throughout history, see: Griffel (2009).

he combined the two categories, in his famous book *al-Mustasfa*, into one, and established the ultimate structure of essentials (Raysuni 2011:19). Nevertheless, he did not clarify why he had chosen this ordering apart from putting the preservation of faith at top since he considers it to function as an umbrella over the rest. However, he gives priority to one essential over another in the circumstance that if any of the consequences of two or more essentials contradict each other or create opposite implications, one must suggest the one which has the higher order necessity to assign priority (Attia 2007:21; Auda 2007:18).

Some of the modern *maqasid* theorists who aim to embody popular contemporary issues - such as freedom, justice, women's rights, democracy, economic development *etc*. - into their *maqasid* theories criticise al-Ghazali by claiming that his *maqasid* understanding is no longer sufficing to meet the objectives mentioned above in his *maqasid* framework (*see*: al-Khamlishi, quoted in Attia 2007:84). These indeed should not be neglected and the *maqasidi* perspective should internalise such matters as well. However, they should be considered as the means (*wasa'il*) leading to the fulfilment of certain objectives. This gives rise to a heated debate about the differentiation of means (*wasa'il*) from the intents (*maqasid*) as some contemporary Islamic legal jurists fall into mistake due to their inability to differentiate means from intents. This issue is discussed at length later.

4.2.2.3. Sayf al-Din al-Amidi (d.631/1234)

al-Amidi assigned the primary function of *maqasid* to be the distinguishing criteria for the rationale of giving preference, namely *al-tarjih*, to certain rulings against another. His *maqasidi* way, by prioritising one ruling amongst others, has been utilised particularly in the resolution of conflicting analogies. Furthermore, through benefiting from the methodology of *al-tarjih,* he attempted to give an ultimate internal ordering for the essential *maqasid* coupled with his general ordering of unanimously and traditionally accepted *maqasid.* In doing so, first he confined the essential *maqasid* to five by stating that there is no other essential objective of Islamic law (Attia 2007:77), and then ordered the essential *maqasid* in such a way that the top priority is given to the preservation of religion (Kamali 2008:11; Raysuni 2011:23). *Usul* scholars, following al-Amidi, interiorized the confinement of essential *maqasid* into five, and explicitly applied this rule in their writings.

4.2.2.4. Al-Izz ibn Abd al-Salam (d.660/1209)

al-Izz developed his theory of *maqasid* by coupling *maqasid* with *maslahah* and *illah* aspects (Kamali 2008:11). In his renowned work and seminal book *Qawa'id al-Ahkam*, al-Izz devoted his entire book to the objectives of Islamic law. His approach to these objectives is based on *maslahah* methodology, which pays particular attention to the achievement of benefit/interest and prevention of harm/mischief. Thus, his core understanding by *maslahah* and *maqasid* relates to the verse (16:90) in *Qur'an*, which roughly states that 'God enjoins doing good deeds and forbids all that are shameful'. In this respect, al-Izz considers the ultimate objective of the Islamic law to be warding off harm and achievement of benefit (Attia 2007:99; Raysuni 2011:32). Within his considerable contributions through introducing the concepts of interest and mischief at the heart of *maqasid* theory, al-Izz expanded the horizons of the theory of *maqasid*, and *maslahah* in general.

Through such a lens of benefit/harm cross-purpose, it can be stated that al-Izz adopted 'objective criterion' (Attia 2007:47), as contrast to the formalistic criterion that is explained later, which basically functions as a filtering mechanism over deciding about how rulings should be associated with one of the three categories – essentials, exigencies and embellishments. In particular, objective criterion necessitates the categorisation of objectives based on their degree of benefit or harm reflected within the rulings. In other words, if the legal ruling stimulates a significant benefit or leads to warding off serious harm, then, objective criterion puts that ruling into one of the categories of higher necessities - exigencies or embellishments.

In line with his extensive investigation of benefit and harm, al-Izz stated that the validity of rulings hinges upon their purposes. If a ruling, one way or another, does not meet its purpose, it should be treated as void (*see*: Auda 2007:19). Lastly, al-Izz influenced the thoughts of al-Qarafi, one of his followers, though al-Qarafi critically approached al-Izz's views and theory.

4.2.4.5. Shihab al-Din al-Qarafi (d. 684/1285)

As the title of his book, *al-Furuq* (*The Difference*), clearly mentions, al-Qarafi's theory of *maqasid* adopts certain methodology that differentiates the intents of Prophet Mohammad's actions with a certain manner. His theory entails that some actions of the Prophet is due to him being the conveyer of the message/revelation, and some other actions associated with his role in the society as a governor, leader or judge. Therefore, the intents of his actions under the former capacity, that is to be the conveyer of the message, must be separated from the intents that are associated with what he does or says as a governor, leader or judge. The intents with the first one must be accepted as a 'general and permanent ruling', while the second one must be categorized under his capacity of being a leader (Auda 2007:19).

As can be seen, al-Qarafi reiterates the distinction between the intents of Prophet that are independent from time and place, and those intents that are specific for certain decisions as a result of particular circumstances. It is for this reason "the Companions used to make a clear distinction between the commands of God's Messenger that ensued from his position as legislator (*maqasid al-tashri'*) and those that did not. When they were not sure about a certain matter, they sought clarification about it" (Ibn Ashur 2006:33).

Al-Qarafi also expands his theory of *maqasid* by introducing 'opening the means' discourse into the *maqasid* agenda. Traditional *maqasid* theories mostly use the idea of 'blocking the means' (*sadd al-dhara'i*) in order to investigate wisdom or purposes of rulings, but al-Qarafi goes beyond the negative side of 'blocking' and incorporates the positive side of 'opening' into the methodology. Thus, his methodology entails that while such means that pose unlawful or prohibited consequences must be blocked out of the *maqasid* agenda, those means that bring out lawful and good ends must be opened (Auda 2007:19). In other words, the rationale for this statement comes from the fact that if the paths are obstructed once they lead to harm, the paths that generate benefit must be opened. This approach is vital in the sense of producing theoretical underpinnings of a proper *maqasid* theory, and *maqasidi* methodology for IBF sector, in particular, for conducting 'opening the means' methodology can lead to solve much-debated deadlocks of IBF sector.

Some scholars claim that al-Qarafi, different from the orthodox tendency of designating essential *maqasid* with five necessities, adds a sixth essential as honor (*al-'ird*) (*see*: Attia 2007:117; Kamali 2008:11). In fact, this attribution is under dispute, since some other scholars ascribed that al-Qarafi just mentioned, in his writings, that some jurists added the sixth dimension as the preservation of honor, without this being his personal view (*see*: Ibn Ashur 2006:118; Raysuni 2011). The second view seems more accurate after reading his passage about honour (*see*: Raysuni 2011:28).

Lastly, al-Qarafi's views on the importance of knowledge of *maqasid al-Shari'ah* are quite worth stressing. He advocates that not only those who give *ijtihad*, independent reasoning, have to acquire the knowledge of *maqasid*, but also those jurisprudents that prefer imitation or emulation of their ancestors must also have such knowledge, lest these jurisprudents issue *fatawa*[45] with a lack of *maqasidi* knowledge (Raysuni 2011:330).

[45] Singular: *fatwa*; it is a legal opinion issued by a highly qualified scholar of Islamic law, or by *mufti*.

4.2.4.6. Abu Ishaq al-Shatibi (d.790/1388)

Together with the contributions of Islamic legal theorists such as al-Juwayni, al-Ghazali and al-Qarafi, the theory of *maqasid* is indebted to al-Shatibi for his great contributions to the theorisation of it. In the first instance, he expanded the horizon of *maqasid* by introducing 'three substantial ways' (Auda 2007:12) that gave rise to the systematisation of *maqasid* theory and enabled scholars to ponder upon *maqasid* in a coherent way. First way is to think the scope of *maqasid* out of the *maslahah* realm and take *maqasid* into the context of 'fundamentals of law' in its own right. Accordingly, he advocated that a high priority should be given to *maqasid al-Shari'ah* over *usul al-fiqh*, since the former has basic roles and characteristics. In the second way, al-Shatibi considers *maqasid* to be the base for the ruling rather than the wisdom behind that ruling. Lastly, he placed the 'certainty' criterion for the derivation of *maqasid* in his authentic inductive process. These three novel ways in developing *maqasid* theory have been utilised by many scholars up until now.

In an attempt to approach to the primary and secondary sources of Islam with the lens of purpose orientedness, Al-Shatibi makes a clear distinction between acts of worship (*ibadat*) and worldly transactions (*mu'amalat*). According to him, 'literal compliance' should be adopted as a methodology in the space of *ibadat* – as Prophet's command about jogging around *Ka'ba* with unclothed shoulders is an example of this assertion, but the consideration of intents or purposes or, namely, consequentialism orientedness should be the exclusive methodology in *mu'amalat* area (Auda 2007:12). This distinction is quite sound and can be employed into the methodology of *maqasid* based economic development index, as vital for the evaluation of IBF performance in an attempt to redefine the meaning and objectives of IBF.

Along such important matters, al-Shatibi also delved into some other main issues in tandem with the theory of *maqasid,* which is extensively scrutinised by Ahmad al-Raysuni in his book: '*Imam al-Shatibi's Theory of the Higher Objectives and Intents of Islamic Law*' (2011). Al-Shatibi's authentic approach and methodology to *maqasid al Shari'ah* discourse has become the most referenced source for contemporary Muslim jurists.

4.2.4.7. Muhammad al-Tahir Ibn Ashur (d.1325/1907)

Ibn Ashur, one of the significant *maqasid* theorists in the modern reformist stream, is presumably the first scholar who developed his theory of *maqasid al-Shari'ah* as a standalone discipline or an independent science (*ilm maqasid al-Shari'ah*) that must be approached outside the realm of *usul al-fiqh*. Ashur's stance with regard to the revival of Islamic law in the modern period renders less emphasis on *usul al-fiqh* but aims to achieve an authentic methodology that finds its theoretical roots in the theory of *maqasid.* In doing so, he severely criticised the traditional schools of Islamic law, since, according to him, these schools could not conceive *maqasid al-Shari'ah* in a purposeful way, but rather treated it as the by-product of *usul al-fiqh* (*see*: Ibn Ashur 2006:xv).

Some modern scholars' responses to this assertion are severe, but to mention Raysuni and Attia briefly, Raysuni (2011:366) is indifferent between tackling *maqasid* as an independent discipline and considering it under the theme of *usul al-fiqh* as long as everyone gives the 'utmost care' to the theory of *maqasid*. However, Attia (2007:244) eschews this tendency of separating *maqasid* from the realm of *usul al-fiqh* and asserts that both *usul al-fiqh* and *maqasid* would be harmed from the consequences of such a divergence, as *usul al-fiqh* forfeits 'the spirit of *maqasid*', while *maqasid* would, in turn, be relegated to have a lesser degree of functionality without any practical role it has.

Under his conceptualisation of *ilm maqasid al-Shari'ah*, Ibn Ashur proposes a universal *maqasid*, which aims to resolve the individuality drawback and 'preservation' restraint in the Ghazalian notion of *maqasid* understanding. In order to disentangle from the individuality drawback, he widens the scope of *maqasid* by introducing society, nation, and *Ummah* as the determining parameters in the objectives of Islamic law. Thus, he gives higher priority to the objectives that are closely concerned with the *Ummah* at macro level rather than the objectives that remain its context at individual level (Ibn Ashur 2006). Ghazalian motto of 'preservation', Ibn Ashur renders, does not suffice to reflect the overall objectives of Islamic law, hence social dimension of *maqasid al-Shari'ah* must be articulated through delineating *maqasid* as both preservation of *Ummah*'s order and also substantial 'perpetuation' of its wellbeing (Attia 2007:81). Ibn Ashur, hence, develops his *maqasid* discourse in such a way that authenticates 'value' and 'system' *vis-à-vis* al-Amiri's theory of 'punishment' and Ghazalian notion of 'preservation' (Auda 2007:22).

Ibn Ashur utilised al-Qarafi's theory of *maqasid* in a way to develop al-Qarafi's conceptualisation of 'difference' in the intents of Prophet's actions (*see*: Ibn Ashur 2006: Section 6). By using the same logic, he substantiated the 'thematic interpretation' as the primary methodology in his theory through scrutinising the *Qur'anic* stories and other verses under particular themes. Therefore, he adopted "contextual interpretation as a new methodology of exegesis" (Auda 2007:254). It is a clear fact that Ibn Ashur had pioneered developing *maqasid al Shari'ah* in new ways which contemporary jurists and scholars to follow.

While Ibn Ashur' - and others' contributions to the *maqasid* theory are essential, in the postmodern era there is no unanimous method for *maqasid* to be implemented on the scriptural rulings. Disputes on methodological issues and even on the characterisation of *maqasid* necessitates that the theory of *maqasid* has to be dealt with a systems approach.

4.3. METHODS IN *MAQASID AL-SHARI'AH* POSITIONING

As discussed above, prominent scholars of Islam in the early centuries of Islam conceptualised and constructed their *maqasid al-Shari'ah* frameworks within authentic frame. Their application of certain methodologies, at the same time, inherited a vast array of literature on methodology to the modern *maqasid* theorists. Since the Ghazalian *maqasidi* understanding, amongst others, has gained the utmost importance in the theorisation of *maqasid al Shari'ah*, the categorisation and establishment of the order of *maqasid* within the frontiers of Ghazalian viewpoint has remained the principal methodological objective throughout the centuries. Thus, the articulation of *maqasid* into the Islamic philosophical sciences has paramountly been attempted with the Ghazalian description.

Islamic economics' argument for developing solutions to the so-called backwardness of Muslim countries and to the state of lack of intellectual acumen relates to bringing the proper methodology of *maqasid* into the modern social sciences. In doing so, most Muslim scholars repeated the traditional *maqasid* methodology, yet some other modernist reformists - including, Mohammad Abduh, Rashid Rida, Ibn Ashur and Yusuf al-Qaradawi - have opened new ways for the articulation of *maqasidi* understanding *vis-à-vis* the modern social sciences.

This section, hence, first elaborates on widely used categorisations of *maqasid* and then vitalises the function of *ijtihad* in energising and renewal of Islamic thought through reflecting on the modern methodological positioning in the *maqasid* discourse. By doing this, it is aimed to introduce both the traditional and modern approaches to *maqasid* methodologies so that a substantial and distinctive methodology of *maqasid al-Shari'ah* can be essentialised in harmonising them within the Islamic moral economy approach.

4.3.1. Categorisation of *Maqasid*

Gamal el-Din Attia (2007), one of the seminal contributors in the modern period, differentiates between the intents of creation (*maqasid al-khalq*) and the higher intents of the Islamic law (*maqasid al-Shari'ah al-'aliyah*) by referring to the view of al-Shatibi, which states that these two intents should be considered under separate titles (Attia 2007:92). However, Attia also provides evidence from certain verses in the *Qur'an* in order to highlight the inseparability of these two intents. Thus, while his categorisation of *maqasid* puts special emphasis on the differentiation of the two intents, he does not imply to consider them in totally different realms.

In considering the legal intents, Attia (2007) identifies 'higher or general intents' which can roughly be identified, as those intents that have the highest ranking and priority amongst other legal intents. His extensive conceptualisation of the higher intents can be explained as follows (Attia 2007:105):[46]

> The higher intents of the Law are embodied in the worship of God [*Tawhid* and *Rububiyyah*], acting as His vicegerents on earth [*Khilafah*], and populating and developing the earth through faith and its requirements [*Imaar*, *Islah,* and *Fard*]. Such requirements of faith include righteous action which achieves happiness both in this life and the next [*Falah*], which encompasses both the material and spiritual aspects of existence [*Amanah*], and which strikes a balance between the interests of the individual and those of society, between particular national interests and the interests of humanity at large, and between the interests of the current generations and those of generations to come [*Rububiyyah* and *Tazkiyah*]. All such intents, moreover, find their expression on the respective levels of the individual, the family, the *Ummah* and all of humanity.

We can infer some Islamic axioms from Attia (2007) as expressed above, namely *Tawhid*, *Khilafah, Islah, Fard, Amanah, Falah*, *Rububiyyah*, and *Tazkiyah*. Thus, this conceptualisation is quite favourable to utilise for implementing *maqasid* on the IBF institutions in constructivist manner within Islamic ontology.

Attia's (2007) higher *maqasid* framework has three subthemes, which are universal intents (*maqasid al-Shari'ah al-kulliyyah*), special intents (*maqasid al-Shari'ah al-khassah*), and particular intents (*maqasid al-Shari'ah al-juz'iyyah*). The universal *maqasid* takes the broadest place in the scope of the intents of Islamic legal rulings. In this sense, it embodies the Ghazalian five level *maqasid*, and, in comparison with the higher intents, universal *maqasid* is considered to be clearer and 'less abstract' (Attia 2007:107). Specific *maqasid*, on the other hand, deals with 'particular divisions' of the Islamic legal rulings as can be exampled by al-Tirmidhi's writings on the secrets and intents of prayer, pilgrimage, *zakah etc*. (Attia 2007:113). Lastly, particular *maqasid* refers to the exploration of those intents in the 'particular legal rulings', which is identified as wisdoms, causes or basis of that ruling (Attia 2007:115). It is clear that Attia's framework of *maqasid* classification is a variant of the orthodox binary classifications; however, his definition of higher intents, in the theoretical sense, can be embedded into the institutional bodies of IBF sector.

[46] The axioms between brackets are introduced by the author to highlight the axiomatic articulation of the statements.

In relation to the traditional categorisation of *maqasid,* known as the five essentials, Attia (2007:64) approaches to this popular tendency in a critical manner by stating that the dynamic categorisation of means (*wasa'il*), in which persons, time, place and circumstances are concurrently considered as determining dimensions of constructing a level based *maqasid* framework, must be established in the scope of *maqasid*; which can, in turn, provide the 'relativity of application' that leads to obviate adopting a fixed categorisation scheme. This multidimensional approach eventually leads him to shift from the five universals to what he develops as 'four realms', namely the expansion of five-limited essentials to a broader twenty-four essentials, which are clustered and distributed under four realms: that is the realm of (i) individual, (ii) family, (iii) the *Ummah*, and (iv) wider humanity (Attia 2007). Although it seems, at first sight, that the expansion of the four realms were arranged one dimensionally, that is the reflection of the mere consideration of the scope of people, in fact, each essential accompanies and embodies with the fundamental issues such as the institutional organisation of the *Ummah*, establishment of justice, preservation of morals, cooperation, solidarity and shared responsibility, dissemination of knowledge, populating and developing the earth and *etc*. Since the elucidation of the twenty-four essentials goes beyond the scope of this research, it is pertinent, here, to mention the essentials.

In rendering a synthesis for the postmodern times, Kamali (2008) blends the historical approaches to *maqasid* categorisation and introduces three types of categorisation within a binary classification method, each having certain mutual contexts. Apart from the classical classification of *daruriyyat*, *hajiyyat*, and *tahsiniyyat*, which is discussed thoroughly in the next subsection, Kamali (2008:6) first classifies *maqasid* into two divisions: general purposes (*al-maqasid al-ammah*) and particular goals (*al-maqasid al-khassah*); where the former functions to characterise the overall *Shari'ah* principles with its most comprehensiveness, while the latter relates to certain subjects and is considered under specific themes such as financial transactions and family issues.

Second classification of *maqasid*, Kamali (2008:7) states, reveals definitive goals (*al-maqasid al-qattiyyah*) and speculative purposes (*al-maqasid al-zanniyyah*). Accordingly, definitive goals are deduced from the explicit evidences in the fundamental sources that are *Qur'an* and *Sunnah*. These *maqasid* are definite in terms of scholars' agreement and being almost no dispute on them; whereas speculative *maqasid*, hence the name implies, lead to some controversies amongst scholars owing to its ambiguity in reflecting the rulings or its derivation from the secondary sources. Kamali (2008) gives the example of al-Shatibi's categorisation, which similarly brings out 'the purposes of the Lawgiver' (*maqasid al-shari'*) and 'human goals' (*maqasid al-mukallaf*), to provide further clarity for this type of classification. The third binary classification aims to differentiate between the 'primary objectives' (*maqasid al-asliyyah*) and 'subsidiary goals' (*maqasid al-tab'iyyah*) (Kamali 2008:7). The former *maqasid* refers to the basic and fundamental purposes of a certain ruling such as it is intended, with marriage, to prevent degeneration of family ties and grow progenies to sustain human life. The 'subsidiary goals', then, features to complement the primary objective of the ruling, as with the example of marriage it also leads to personal gratification.

Being a main contender in the theory of *maqasid* in the contemporary times, Auda (2007) presents a thorough synopsis of various *maqasid* categorisations. He, first, identifies some dimensions within which *maqasid* classification is constructed. These are (Auda 2007:3):

(i) Levels of necessity, which is the traditional classification;
(ii) Scope of the rulings aiming to achieve purposes;
(iii) Scope of people included in purposes;
(iv) Level of universality of the purposes.

Although three levels of necessities are embraced, to a large extent, to be consisting of *daruriyyat*, *hajiyyat*, and *tahsiniyyat,* Attia (2007:42) proposes a 'five level necessities framework' in which he introduces, as a result of his interpretation of Suyuti's relevant views, 'utter necessity (*darurah*), need (*hajah*), benefit (*al-manfa'ah*), embellishment (*al-zinah*), and surfeit (*al-fudul*)' as more proper and all-embracing *maqasid* framework. This framework, in the sense of identifying levels of necessities, would be more explicative than the prevailing identification of necessities. However, as mentioned briefly before, traditional classification of *maqasid* provides three levels of necessities: *daruriyyat*, *hajiyyat*, and *tahsiniyyat.* Each necessity has a hierarchical relationship in its own right in which *daruriyyat* embodies the most essential part to be fulfilled; then *hajiyyat*, and *tahsiniyyat* are satisfied respectively. In critically reflecting, rather than considering it as an entire paradigm, Ghazalian five level *maqasid* falls under the *daruriyyat* category in which preservation of faith, human life, faculty of reason, progeny, and material wealth are recognised as the fundamental objectives that the Islamic scriptural sources aims to fulfil. However, contemporary legal theorists argue that the traditional classification has some substantial drawbacks, which fall short of producing robust solutions especially in contemporary times. Some of the criticisms levelled are as follows (Auda 2007:4):

(i) the scope of traditional *maqasid* might remain incapable to reflect specific intents of particular rulings due to the adaptation of revealing general *maqasid*;
(ii) the individuality drawback which is mostly referred to the Ghazalian *maqasid* framework, as it claimed that the existent five level *maqasid* does not include societal or *Ummah* level objectives;

(iii) traditional *maqasid* lacks 'the most universal objectives' such as 'justice', 'development' and 'freedom';

(iv) traditional *maqasid* is constructed based on 'the *fiqhi* literature, rather than original sources.

In addition, 'safeguarding' as opposed to 'proactivity of development' should also be considered as an important handicap of Ghazalian frame in developing a developmentalist outlook within IBF.

Based on these criticisms, modern scholarship has opened new ways to rediscover and enhance the existent classification of *maqasid*, which would ideally overcome the inherent flaws of traditional categorisation. One of the ways in constructing proper *maqasid* refers to the scope of the rulings; that is the general, specific and partial *maqasid*. 'General *maqasid'* identifies itself with the entire sources of Islamic law, which embrace the five level necessities together with the newly introduced concepts such as justice, human rights and freedom. 'Specific *maqasid'*, with a narrower sense, pertains to those *maqasid* that is induced from certain chapters of sources of Islamic law; for instance, the prime issues in the family and inheritance law and *etc*. Lastly, 'partial *maqasid'* is concerned with the intents that specific scriptural rulings aim to reveal out. This can be exemplified with the allowance of breaking one's fasting due to specific personal circumstances.

In an attempt to challenge the individual-based theorisation of *maqasid*, some scholars in the modern period attempted to incorporate societal or wider aspects of Islamic rulings into the scope of *maqasid* to avoid individualistic nature as a drawback. In this manner, Ibn Ashur gave precedence to *Ummah*-concerned *maqasid* against individual-concerned *maqasid*; by the same token, Rashid Rida introduced the concerns of women's rights and reform in theorising *maqasid*, and lastly, Qaradawi reiterated the importance of freedom, social welfare and human dignity as important concerns for *maqasid* (Auda 2007:5).

The third categorisation aims to circumvent 'the historicity of *fiqh* literature' on *maqasid al-Shari'ah* and introduces new universal objectives that are induced directly from original sources, rather than from the *fiqhi* knowledge repository. These universal objectives attach itself basically to such issues of social welfare, development, human rights, improving the quality of research and development, human fraternity and *etc*.

After his clarification, Auda (2007) reiterates the one-dimensional nature of each of these categorisations. Instead, he urges a multidimensional structure, as part of the systems philosophy, which encompasses all the aspects mentioned above. In other words, a multidimensional approach essentialises the “levels of necessity, scope of rulings, scope of people and levels of universality” (Auda 2007:8) all together in order to structure *maqasid al-Shari’ah* substantively. Such a comprehensive multidimensionality is discussed later, as one of the main foundations in articulating *maqasid* into IME within the systems approach.

Lastly, as reported by Attia (2007:87), Yahya Muhammad makes a distinction between the *ta’abbudi* rulings that is “rulings for which there is no rationally discernible purpose” and the rulings about judicial interests (*al-masalih al-huquqiyyah*). In this lens, he criticises the Ghazalian five universals and urges the ultimate intents (*al-maqasid al-gha’iyyah*) instead. Accordingly, he claims that the five universals are concerned with ‘peoples’ material interests’, while the ultimate intents are the ‘true intents’ that incorporates such distinctive objectives of “worship and devotion (*al-ta’abbud*), prudence (*al-ta’aqqul*), emancipation (*al-taharrur*), assuming the traits [of the Divine] (*al-takhalluq*), unification (*al-tawahhud*), and perfection (*al-takammul*)” (taken from Attia 2007:87). While Muhammad’s proposition conceptually addresses the straight objectives, the chief question still remains as to how these objectives can be substantiated within a socioeconomic base thereby their articulations in socio-economic life can fulfill *maqasid al-Shari’ah*.

4.3.2. The Role of *Ijtihad* as the Catalyst in the Making of *Maqasid al-Shari’ah*

The articulation of *ijtihad* with the concept of *maqasid* reveals the *maqasid*-based *ijtihad*, which is a recent conceptualisation that has been used to enlarge the scope of *maqasidi* thinking. In the modern period, *maqasid*-based *ijtihad* has been given special importance by Raysuni (2011) who attaches four principles in order for it to function smoothly. These principles, respectively, are (Raysuni 2011:Chapter 4-Section 2):

(i) inseparability of texts and rulings from their objectives;
(ii) combining universal principles and evidence applicable to particular cases;
(iii) achieving benefit and preventing harm; and lastly
(iv) consideration of outcomes.

As can be inferred directly, the first principal rejects the literalist or textualist approach to the sources of Islamic law by bringing the dynamism of independent reasoning (*ijtihad*) especially for the circumstances in which literalist methodology does not suffice in deducing the objective from certain ruling. In addition, the fourth principle evokes the consequentialist adaptation in the sense that the consequents as the outcome of *maqasid*-based *ijtihad* must also comply with the substance of *Shari’ah*.

It is argued that *ijtihad*, as a mechanism functioning for the renewal of Islamic legal thought, would also sweep away the inclination of arbitrariness or the unbridled intellectual reasoning in the identification of *maqasid* (Attia 2007:161). Precisely, the scope of *maqasid* is exposed to biased interpretations and identifications, which would result in arbitrary justifications that are far from the substance of *maqasid al-Shari'ah* understanding. Thus, collective *ijtihad* would ensure the eschewal of this arbitrariness. To generalise, there is a bidirectional relationship between *ijtihad* mechanism and the knowledge of *maqasid*, which feeds upon each other. Thus, producing certain *ijtihad* necessitates the deep knowledge of *maqasid*, for *ijtihad* functions at the core of the *maqasid* theorisation.

Similar to any other discipline, in the IBF field, decision-making process through *ijtihad* mechanism primarily requires the knowledge of *maqasid* amongst decision makers. Since the knowledge of *maqasid* has not been acquired properly or narrow construction of *maqasid* adopted among the Islamic scholars in the contemporary times, pseudo-*ijtihadi* decisions are being relied upon though it does not produce substantial outcomes. Thus, the embedment of *maqasidi* thinking into the social sciences, such as Islamic economics and finance, would be the principal objective.

4.4. *MAQASID AL-SHARI'AH* AND DEVELOPMENTALISM IN ISLAMIC POLITICAL ECONOMY FRAMEWORK

With the aim of reconstructing social formation of post-colonial Muslim societies through establishing advanced institutions and creating an authentic Muslim identity in the post war period, the idea of Islamic economics was essentialised and theorised within a developmentalist agenda. By doing so, developmentalism with public policy orientation has taken principal position in the constitution of Islamic economics paradigm with the objective of eliminating underdevelopment, impoverishment and weak politico economic elbowroom that are drastically suffered in the Muslim societies.

Since IBF emerged as the main institutions of Islamic economics paradigm beyond the traditional social welfare institutions, IBF, as discussed in Chapter 2, has been attributed the role of financing development in the Muslim societies. However, despite the unprecedent growth in IBF assets and transactional size in recent years, one of the main debates has been the substantive failure of IBF in terms of failing to contribute to socioeconomic development or societal transformation due to various reasons including opting for financialisation as discussed in Chapter 3. This chapter, as stated previously, considers *maqasid al-Shari'ah* related understanding as another reason for the observed developmentalist failure (*see*: Asutay 2007, 2012). Therefore, this section aims to bring the methodological debate to the surface around *maqasid al-Shari'ah* in line with the theoretical debate presented above.

4.4.1. The Failure of *Maqasid*-based Approach to Developmentalism

In tandem with developmentalism objective, founding fathers of Islamic economics utilised certain *maqasid al-Shari'ah* framework, which is mainly located in the theoretical expression of al-Ghazali's structure, in order to identify and articulate developmentalism with the objectives of *Shari'ah*. Consequently, in that imagination, Islamic economics would achieve and sustain developmentalism through a structured *maqasid* methodology. However, due to the prevailing financialisation trend across the world and the urgent need for the enhancement of financial institutions in the Muslim world, the orientation of theoretical studies in Islamic economics gave way to the quest for institutionalisation process of IBF sector. In this pragmatic positioning, *maqasid al-Shari'ah* has been relegated to render legitimacy in an instrumental manner for *Shari'ah* compliancy in a formalistic way at best. In the wake of a shift from the ideals of Islamic economics to the realities of IBF, the close link between developmentalism and *maqasid al-Shari'ah* has been broken for the sake of yielding efficiency in the practices of IBF institutions. In contrast to the expectations, these institutions eventually led to the malaise of IBF, and considered to be the 'second best solution' (Asutay 2007b, 2012) in relation to developmentalist objectives.

Despite the fact that the general trend of Islamic economic studies has been moving towards unsophisticated and non-theoretical making of Islamic finance, Islamic moral economy, on the other hand, reiterates the indissociably strong nature nature between developmentalism and *maqasid al-Shari'ah*, such that the latter functions as the substantial methodology for the former in identifying the mechanism and methods of achieving the particularities of Islamic economics by delivering Islamic moral economy in the end. Otherwise, promoting the prevailing understanding of *maqasid* shaped by the impositions of market driven economic system would not generate the desired structural transformation in the societal level. Thus, it is argued by this research that the authenticity of institutions including IBF and the reformulation of Muslim identity can be accomplished through a proactive *maqasid* understanding. To achieve this, the embedment of *maqasid al-Shari'ah* into Islamic economics has to be fulfilled to substantiate the formation of Islamic moral economy beyond the *fiqhi* or *maslahah*-based Islamic financialisation, which is an objective pursued and explored in this study.

4.4.2. *Maqasid* in Islamic Economics and Finance: A Review of Literature

It seems at first glance that *maqasid al-Shari'ah* has always been treated as an essential concept around which the theory of Islamic economics has been constructed, and IBF services have been put into practice. While it is true that the founding fathers of Islamic economics, such as Chapra (2008), among others, put great emphasis on *maqasid* from the very beginning to provide a methodological base for theory construction; subsequent contenders, practitioners and policy-makers of Islamic finance have given recognition to its significance quite recently. A quick survey of the relevant literature affirms this observation, as the majority of *maqasid*-related articles and books were written in the last ten years, leaving a great gap between mid-1980s to 2000s.

Comparing the initial expressions by the founding fathers and the recent understanding developed, it is evident that *maqasid* has been wrested from the wider arena of Islamic economics to be downsized to the sphere of Islamic finance. In this section, a survey of the *maqasid* related literature on Islamic economics and finance is presented in two subsections. The first subsection depicts quite extensively the emergence and essentialisation of *maqasid al-Shari'ah* within Islamic economics in the works of the founding fathers, while the second focuses on the espousal of *maqasid* in the prevailing applications of Islamic finance. Thus, the divergence between theoretical and empirical studies is brought to the fore by showing how the theoretical articulation of *maqasid* is projected in practice.

4.4.2.1. Maqasid al-Shari'ah and Islamic economics: early contributions

With the rise, expansion and institutionalisation of modern sciences since the 17th century, Western philosophy experienced a radical shift from teleology to causality, which crystallised causal reasoning as the core of modern sciences in the face of teleology that basically explains a phenomenon in terms of its function and 'purpose'. More precisely, modern Western philosophy, with its dominant positivist inclination, has been constructed exclusively within the 'cause-and-effect' dialectic within the framework of mechanistic explanations of natural and social phenomena, which entails causality and causal explanation as the central logic of thinking. Therefore, teleological orientation in any theory or idea has been regarded as metaphysical, nonsensical, and hence completely rejected (for an extensive discussion on this, *see*: Auda 2007:27).

In contradistinction to positivist understanding, and in the context of Islamic philosophy and worldview, *maqasid* al-*Shari'ah* suggests a different understanding through its purposefulness and goal-seeking approach by embedding 'theologically' defined developmentalist ends in the relevant knowledge development process and practice. In this respect, the founding fathers of Islamic economics attempted to detach themselves not only from the modern positivistic scientific methodology engulfed in the cause-effect nexus and mode of thinking, but also from the postmodern understanding, which proposes deconstruction of any sort of centrism (de-centring) and universal truth constructions revolving around rationality assumptions.

Of the pioneering scholars of Islamic economics, Chapra's (2008) contributions in particular have played a significant role in guiding and inspiring following generations by emphasising the concept of *falah* or real well-being which constitutes the ultimate goal of the teachings of Islam. Such well-being, Chapra (2008) maintains, cannot be attained merely by the satisfaction of just the material needs of the human beings, a matter that depends on the level of income and wealth. Rather, there are other needs that have to be fulfilled, most of which are spiritual and non-material in character and need not necessarily become satisfied as a result of increase in income (Chapra 2008:1). Placing individual *falah* at the centre of his theorisation, Chapra (2008) adopts the essential taxonomy of *maqasid* articulated by al-Ghazali and upheld by subsequent Muslim scholars and jurists, especially the five universal necessities which consist of the safeguarding of faith (*din*), the human self (*nafs*), intellect (*'aql*), posterity (*nasl*) and wealth (*mal*). Within the framework of these core values, spiritual and non-material needs of the individual are given essential consideration in determining the goals of the Islamic economic system.

Chapra (2008), however, admits that these five taxonomy as delineated by al-Ghazali are not the only *maqasid* aimed at ensuring human well-being; there are many others stated in the *Qur'an* and the *Sunnah* or inferred from them by many scholars. For Chapra (2008), while these five can be seen as primary *maqasid* (*asliyyah*), the others may be considered as their corollaries (*tabi'ah*). The realisation of the corollary *maqasid* is necessary as means to the realisation of the primary ones. Furthermore, the primary *maqasid* are unchanging and constitute ends in themselves, whereas their corollaries are flexible "and may keep on expanding and changing with the passage of time" (Chapra 2008:4). In Chapra's categorisation, the corollaries reflect the inherent dynamism of the *Shari'ah* and they are such that enable us "to ensure that all human rights are duly honoured and that all the different human needs are adequately satisfied" (Chapra 2008:5). Both categories are constituted in such a manner that human beings are seen as "the end as well as the means of development" process.

Chapra's restructuring of *maqasid* into the real economy and economic development realm, relies basically on strengthening the five universal necessities or essentials, namely the human self, faith, intellect, posterity and wealth, through fulfilling a set of corollary objectives. For example, Chapra (2008) underlines the cruciality of policy goals geared towards attaining security of life and property, removal of poverty, employment and self-employment, equitable distribution of income and wealth, education, good governance and development and expansion of wealth, all of which should result in the invigoration of the human self (*nafs*) which is one of the five primary objectives of the *Shari'ah*. Similarly, the enrichment of faith requires the establishment of certain 'rules of behaviour (values)' and 'proper motivation' within Islamic worldview. Significantly, Chapra's reformulation of the theory of *maqasid* brings forward two very important features: one has to do with his espousal of the notion of 'enrichment' or 'invigoration' instead of the classical scholars' idea of 'preservation' or 'safeguarding' in delineating the five essentials; the other aims to incorporate societal aspects of *maqasid*, through corollaries, in relation to its economic dimension.

It can be deduced from the foregoing exposition that Chapra (2008) purposes a reformulation and extension of the notion of *maqasid* grounded in the Ghazalian basic structure whereby special emphasis is put on the social and development dimension giving it a wider scope and more dynamic character expressed by such terms like 'enrichment' and 'invigoration'.

Siddiqi (2010), another eminent figure of Islamic economics, approaches to the objectives of *Shari'ah* in a comprehensive manner in his quite recent book *Maqasid e Shariet: Ek Asri Mutala*[47], in which he mainly argues that contemporary Islamic scholars have mixed up *Shari'ah* objectives with the objectives of *fiqh,* as the intense academic debate evidences this fact in their writings. Thus, he suggests that those scholars confine entire objectives to *fiqhi* rulings *vis-à-vis Shari'ah*. In addition to this, contemporary *maqasid* theories appropriated the renowned Ghazalian *maqasid* structure, which, according to Siddiqi, must be enriched by incorporating the insights of Ibn Taymiyya and Ibn Qayyim al-Jawziyyah. The views of these two scholars constitute an important element in Siddiqi's *maqasid*-oriented thinking: Ibn Taymiyyah suggests considering securing benefits (*masalih*) as one of the main goals of the *Shari'ah*, to which Ibn al-Qayyim adds justice as essential objective. By invoking these two scholars and incorporating their views in his conception of *maqasid*, Siddiqi (2004a) makes it clear that he rejects the idea of capturing the objectives into a finite list.

[47] The book is written in Urdu language and has not been rendered into English yet. Despite this limitation, it is possible to have an overview of the book thanks to its scholarly review by Abdul Azim Islahi (2010).

Favoring Ibn al-Qayyim's ideas, Siddiqi (2010:239) expands *maqasid* through embedding such objectives of "cooperation at the world level, justice and equity, poverty alleviation, bridging gap between the poor and the rich, sustenance for all, peace and progress, moderation and balance, growth (*tazkiyah*), and justice (*qist*)" into the five essentials. Particularly, in evaluating the state of the IBF sector, Siddiqi (2004b) sees the crux of the problem as the general failure of examining the findings of IBF according to *maqasid al-Shari'ah* criterion. In this manner, Islamic finance operations evidence that *fuqaha* mostly tackles the newly introduced financial products within a narrow perspective as to what their return could be to the supplier, rather than putting their broader consequences into the agenda (as suggested by *tawhid*) and issuing their *fatwas* accordingly. However, as Siddiqi (2010, 2004a) suggests, the principal objective of using *maqasid al-Shari'ah* as the methodology for IBF sector must produce new public policies that reflect the substance of the theory of Islamic economics, and not just mere forms of hybrid products. The ideal *maqasid* methodology, Siddiqi further argues, must fulfil the specific objectives related to IBF sector. Among them, utmost importance should be given to "encouraging businessmen and establishments for taking risks". Further, "justice, equity and benevolence should be necessary ingredients of finance so that not only one party would bear all the negative effects of the partnership and investment" (Siddiqi 2010:239). Otherwise, any process of economic development based on financial operations that are oblivious to justice and benevolence would only lead to "bad consequences" (Siddiqi 2010:239).

Besides the contributions of Chapra and Siddiqi who attempted to develop a wider *maqasid* framework that aims to make *maqasid al-Shari'ah* essential to the methodology and substance of Islamic economics, there are other scholars who took it upon themselves to examine particular subjects in Islamic economics and finance through a general *maqasid* approach. Kahf (2006), for instance, focuses on the *Shari'ah* goals intended by the prohibition of interest (*riba*) and identifies their implications for IBF sector. In light of an explication of the rationale behind the prohibition of *riba* based on evidence from the *Quran* (2:279) and the Prophet's sayings that strictly urge upon forbidding *riba*, Kahf (2006:9–10) proceeds to discuss some certain characteristics that should be observed in IBF products and have to do with their moral soundness, namely avoiding harmful products, *Shari'ah* permissibility of the products, establishing obligational balance between each parties, founding all financing contracts on real exchanges and assets. He, then, elucidates the primary objectives pertaining to the prohibition of *riba* by determining eight objectives, some of which listed below (Kahf 2006:9–10):

(i) Preventing return from being assigned to an asset that does not produce return;

(ii) Avoiding distribution of anything except the real value added or value created in an asset;
(iii) Upholding the sanctity of property rights;
(iv) Disallowing debts trade and exchange along with similarly unrealistic purely speculative transactions that are not based on real production;
(v) 'Preventing' debt discounting and rescheduling for increment.

In Kahf's delineation of the *Shari'ah* objectives in the prohibition of *riba* there is an undeniable protectionist approach that is clearly expressed by such terms as prevention, avoiding, disallowing and upholding have been chosen for the articulation of *maqasid al-Shari'ah*. This approach is indebted, not surprisingly, to the Ghazalian formulation and structuring *maqasid*, which is critically examined in this study in detail in a later section. However, Kahf's *maqasidi* interpretation of *riba* constitutes a novel attempt to the critique of modern IBF practices.

Ahmad (2011), similarly, critically approaches to the role of IBF in fulfilling Ghazalian taxonomy of *maqasid*. His *maqasid* oriented theorisation focuses mainly on 'protection of human life' and 'protection of Islamic religion'; the other three objectives are conceived to support these two cores and complement them. The former objective is built on two complementary *maqasid*; that is 'education' and 'justice' which ultimately pave the way for developing *halal* productive activities, educational and training programs in the financial capacity of markets (Ahmad 2011:6–7). The undertaking of these activities mainly requires the prohibition of '*riba* trade in debt, and *gharar*' so that *halal* ways of production can be established. As for the second objective, it is essential to develop judicial and educational institutions in order to maintain and promote justice. Respect of private property rights, in the same vein, functions for protecting wealth, which plays a complementary role in achieving these objectives.

Ahmad (2011) determines, without much explanation, the chief targets of Islamic finance in its relation to realising *maqasid* through incorporating them into Shatibian three-level classification. Amongst them, the first target, namely low levels of development expressed as *daruriyyat* or essential needs, is addressed by the alleviation of poverty mainly through mobilizing resources and directing them towards sound projects. Second target, medium stage of development in the form of *hajiyyat* or complementary can be achieved through facilitating, for example, better health systems and education and schooling system, and improving infrastructure. Lastly, the high stage of development or *tahsiniyyat* implying embellishment aims at satisfying luxurious necessities of individuals and society as long as it does not produce waste, consumerism and inequality; as having *tahsiniyyat* related consequences leads to improvement and the attainment in individual lives.

Under this structure, Ahmad (2011:15–16) presents some policy recommendations pertaining to the applications of Islamic finance:

(i) Giving up over-dependence on *murabahah* contract;

(ii) Following and even developing the use of new types of contracts that have been first launched by countries such as Sudan, the Gulf states and Malaysia;

(iii) Putting the objective of financing the poor at the core;

(iv) Finding some authentic benchmarks other than interest rates for determining the profit margin;

(v) Expanding *sukuk* operations, but through avoiding some standards of it which have toxic nature;

(vi) Discontinuing *tawarruq* contracts, which, in reality, does not differ much from interest-based loans.

It must be stated that *maqasid al-Shari'ah* has an extensive sphere in terms of shaping IBF; thereby its penetration area can hardly be explained by only protection of wealth, human life and religion. In addition, Ahmad's (2011) structure falls short of articulation of *maqasid* as a methodology, while he well diagnosed the flaws in its applications with IBF. For instance, the way of alleviating poverty, as being one of the objectives of Islamic economics, was explained in an abstract way by using classical suggestions in relation to the role of IBF, such as mobilising resources and directing them into related projects. However, system approach necessitates much broader view on this *maqasid* by surfacing the causes of poverty specific to that society and suggesting proper ways to eliminate it within a political economy perspective.

Ahmed (2011) elaborated a more comprehensive view on Islamic financial products and *maqasid al-Shari'ah* nexus through utilising, what can be identified as, an Ibn Qayyimian *maqasidi* understanding by determining the general objective of Islamic law as promoting or enhancing welfare of mankind as well as preventing and protecting from harm. This implies that "other than fulfilling the legal requirements, an Islamic financial system should also cater to the social needs of a society" (Ahmed 2011:149). Ahmed (2011) suggests two sets of *Shari'ah* requirements – legal and social requirements – as the chief implications of *maqasid* regarding the IBF sector; however, at the same time, he urges acknowledging the difference between these two. Of the legal requirements, Ahmed (2011:151) stresses on 'abiding with the relevant legal maxims' wherein, according to *Majallah* rules, "attention is given to the objects and meanings, not to the words and form" (*Majallah*, 2001; cited by Ahmed 2011:151), 'form-substance harmony' which aims to preclude focusing on form and ignoring substance of Islamic law, 'using ruses (*hilah*)' to produce Pseudo-Islamic products that are unlawful in substance, and lastly 'considering outcomes of the transaction' in a consequentialist manner. It is evident that the legal requirements identified by Ahmed (2011) are in harmony with the spirit of *maqasid al-Shari'ah* with its all-embracing context and complementarity role with social requirements, since it goes beyond narrowed *fiqhi* considerations and substantiates the extensiveness and dynamism of Islamic law with respect to Islamic financial products.

As being complement to the former one, Ahmed (2011) emphasizes the social requirements, which embrace two important dimensions as 'market segment' and 'needs/purposes' that are served by financial products. Market segment mainly functions for serving basic and advanced financial needs of all stakes in the society including household and business sector, small and micro enterprises, and poor and middle-class groups. Needs, on the other hand, has to be satisfied as part of the objectives of IBF; hence, to make it concrete, they are divided into survival needs, security needs, and growth needs (for further discussion, *see*: Ahmed 2011:154) within the scope of IBF. Thus, the realisation of *maqasid* in the IBF field requires the satisfaction of each need in tandem with the market segment concerns and legal requirements in general.

Ahmed (2011), furthermore, identifies three types of products that play a vital role on the realisation of *maqasid*. Amongst them, 'pseudo-Islamic products' are those, which conform to the legal form, but fail to substantiate the substance of Islamic law. Applying ruses (*hilah*) not for exceptional cases, but rather for general practices and contracts (such as organized *tawarruq*) is the obvious example reflecting this kind of products. *Shari'ah* compliant products; secondly, are unable to incorporate social objectives explicated in the social requirements, despite the fact that they fulfil the form-substance considerations. The best practice reflecting the *Shari'ah* compliant products can be of those, which disregard the poor or middle sections of society, because their transaction costs and risks bearings are high, and investment returns are low. Proliferation of these products amongst markets mainly stems from the lack of Ibn Qayyimian understanding within which IBF is constructed and operated, and through which societal consequences are vitalised. Distinct from these two kinds of products, *Shari'ah* based products, thirdly, aim to reach all segments of society and satisfy both survival and security needs of individuals without causing any form-substance dilemma. In this manner, *maqasid al-Shari'ah* can be achieved by endowing *Shari'ah* based products entirely in the financial services. Overall, while it can be further developed in a systematic manner, Ahmed's (2011) approach to *maqasid* and its articulation on product development in the IBF sector has a novel character in methodological senses.

In further exploring the articulation of *maqasid al-Shari'ah* in IBF, corporate social responsibility (CSR) can be considered, as CSR issues have become a central concern for modern corporations and middle scale businesses – as well as for management and finance theorists – in both conventional and Islamic financial institutions. The vitality and functionality of CSR in such institutions is reinterpreted from the *maqasid al-Shari'ah* perspective by Dusuki and Abdullah (2007). They considered fulfilling CSR requirements to be one of the utmost objectives in financial sphere. In doing so, Dusuki and Abdullah (2007) framed their CSR modelling around the Ghazalian *maqasidi* structure, which they believe functions as preserving the public good, through essentialising the five essentials and regarded the notion of 'preventing harm' as significant, since, they thought, Islamic legal maxims were all derived from this principle. Therefore, as the implications of *maqasid* on CSR necessitates, individuals and groups in corporations must behave in a manner that does not undermine their role of being vicegerents (*khalifah*) of, and responsible to the Almighty. In addition, another implication invokes a '*taqwa*-based business paradigm', which does not limit the entrepreneur to seek his profit maximisation, but also requires the fulfilment of moral and social responsibilities that can be realised through considering the wellbeing of all stakeholders in his business (Dusuki and Abdullah 2007:34); thereby Islamic reward system transcends orthodox applications by bringing the other world into analysis.

Dusuki and Abdullah (2007) also reckoned the concept of *maslahah* into the CSR issues by constructing a *maslahah* pyramid that has three levels of necessities. While the first level being *daruriyyat* level requires the preservation and protection of the essential needs of all stakeholders such as protecting employees' welfare, safety and health, *hajiyyat* and *tahsiniyyat* respectively has a role of removing difficulties and hardship (such as offering fair pay and safe workplace, and initiating human quality programs), and engaging social activities that lead to perfect public life such as offering financial help for poor and successful students.

Although the importance of CSR has been popularised among academic disciplines, it has also accompanied with some cogent criticisms within a political economy approach (*see*: Banerjee 2008; Blowfield and Frynas 2005; Vogel 2007; Wang, Choi, and Li 2008). Thus, beyond the idealisation of CSR as the rectifying or consequence moderating instrumental policy over CSR, practical applications evidence capitalist interests in disguise of CSR. Similarly, it is questionable as to which extent CSR is capable of serving both the interest of corporations and that of individuals and society at length, since the *modus operandi* of capitalist system works within the rules of zero sum game and Pareto optimality. Thus, embedding *maqasid al-Shari'ah* into CSR could consider these politico-economic aspects and endeavour to eliminate the zero-sum nature of financial dealings through bringing *tazkiyah* as an axiom under the *tawhidi* framework, which inherently considers the wellbeing all stakeholders of society concurrently due to the *rububiyah* axiom.

Another issue in IBF is the relegation of *maqasid al-Shari'ah* to the objective of preservation of wealth. In this sight, Dusuki and Bouheraoua (2011) determines five main dimensions in which preservation of wealth is achieved through; (i) the protection of ownership, (ii) acquisition and development, (iii) preventing damage, (iv) its circulation, and (v) its value protection. Similarly, Laldin and Furqani (2013) specify three ends in particular for IBF, which are circulation of wealth smoothly, fair and transparent financial practices and justice and equity at both micro and macro levels. These two views among many others unearth the old and inherent debate about the basic role of IBF. Accordingly, one stream argues that the structure of IBF must be regarded similar to conventional banking and finance with respect to functions and basic operations, that is fulfilling financial needs of individuals and channelling individual savings into most efficient investment opportunities, but additionally IBF must embrace and operationalise legal maxims of *Shari'ah* about contractual rules and regulations. Therefore, this view implies that the structure and operational nature of banking and finance is universal, which display the same function due to the nature of a bank being a business entity, hence expecting public policy outcomes from IBF activities is no more than a 'romantic; and 'delusional' view (*see*, for instance, El-Din 2013). Nonetheless, public policy can occasionally result as an outcome, but in an instrumental manner. The reflection of this view in the *maqasid al-Shari'ah* debate necessarily limits itself with the objective of preservation of wealth. However, expanding or, more precisely, shifting the scope of IBF beyond orthodox stereotypes would encapsulate the extensive objectives clarified in both al-Ghazali's and other scholars' *maqasid* frameworks. Otherwise, following the existing structure of banking and finance designated by neoclassical economics necessitates the detachment of its objectives from social dimensions through being 'profit-oriented entities' rather than 'social based ones' (Mohammad and Shahwan 2013).

As surveyed above, the long trajectory of theorising Islamic economics displays features of homogenous and dilatory development. The founding fathers and subsequent scholars in their attempt to construct theories of Islamic economics have benefited from Ghazalian *maqasid* framework, as a methodological framework in defining the objective function, and through non-substantiated attempts. In doing so, *maqasid al-Shari'ah* are essentialised within Islamic economics on the surface, yet the embedment of it as the substantial methodology is mostly missed, and the five-level essentials are favoured with limited articulations. The next section demonstrates how contemporary contenders in Islamic finance have even further narrowed the scope of *maqasid* to the preservation of wealth, which is rather evident in most empirical studies related to IBF.

4.4.2.2. Maqasid al-Shari'ah and Islamic finance: eclecticism and romanticism

Even though *maqasid al-Shari'ah* could not be profoundly embedded in the theoretical framework of Islamic economics in the efforts of founding fathers, their contributions were of great importance since they established the theoretical base, dimensions and objectives of Islamic economics. It is, therefore, expected that the successors would reap the benefits of these contributions in both theoretical and practical field by essentialising *maqasid* as a methodology. However, the political economy of the Muslim world under the existing hegemony has not allowed the emergence of Islamic economics neither as a theory nor a practice as an economic system to flourish and play a central role over leading Islamic financing applications. Thus, the entire institutional authenticity search initiated by Islamic economics in the end has been relegated to IBF, as the capital accumulation resulting from petro-dollars of the 1970s and 1980s urged and expedited the process of establishing Islamic financial industry as an 'integral' sector of the global financial system. In the initial stage, there was not much debate and intervention on the rise of Islamic finance in order to preserve the ongoing profitability. *Maqasid* related debate in the form of substantive morality, therefore, had to wait until 2000s when the social failure of Islamic banking started to be recognised (Asutay 2007b:109, 2012; El-Gamal 2007).

Highly influenced by these historical developments, the infant empirical literature on *maqasid* and IBF nexus basically follows two main trends. The first type of literature stresses the need for a *maqasidi* perspective to remove the social failure of Islamic finance. These studies, hence, in a romanticized manner, highlights the debates on 'form *vs* substance', '*Shari'ah*-based vs *Shari'ah*-compliancy', 'debt finance *vs* equity finance', 'banks as profit-oriented entities *vs* banks as socially-oriented entity' (for an overview of these studies, *see*: Dusuki and Abozaid 2007; El-Najar 2014; Mohammad and Shahwan 2013; Sairally 2015; Soualhi 2015; Zakariyah 2015). Although delineating the aspects of failure considerably important, the debate remained highly limited in the sense of suggesting authentic solutions with *maqasid* lens.

In addition to highlighting the failure in a discursive manner, another step of empirical character was made consisting of the efforts aimed at constructing a *maqasid* index and applying it to economic performances of Muslim dominated countries. Such an exercise aims to diagnose to what extent economies perform in line with the objectives of *Shari'ah*[48]. In terms of measuring economic, social and other performances together, *maqasid* index resembles multidimensional indices such as Human Development Index, Happiness Index, OECD Better Life Index and *etc*.

Table 4.1: Variables for the Ghazalian Five-Level Dimensions

Hifz al-Din	- Religious freedom - Crime rate - Corruption rate - Peace Index
Hifz al- Nafs	- Average life expectancy - Human rights index - Freedom Index
Hifz al-'Aql	- Education - Technology use - Number of researches - Articles published - School enrolment - Spending on education
Hifz al-Mal	- GDP per capita - Household consumption - Gini ratio
Hifz al-Nasl	- Fertility rate - Life expectancy at birth - Health expenditure as percentage of GDP - Divorce rate - Child mortality rate

Note: Developed from the secondary data-based studies

By using *maqasid* index, a number of researches aimed either to measure overall economic performance, or specifically Islamic banks' performance. The common characteristic of the index attempts is the adoption of Ghazalian fivefold taxonomy of *maqasid* framework, which is invariably and extensively utilised in the relevant academic studies. Looking at the country level *maqasid* performance studies, both primary and secondary data are selected in determining the variables for each dimension. Those selecting primary data mostly conduct questionnaires, in-depth interviews, surveys or using directly existing primary data such as World Values Survey and Gallup Analytics. As for the secondary data, World Bank, IMF, UNESCO and UNDP databases are utilised. The most appropriate approximation of the five dimensions are sought in these databases, or surveys and questions are intended to meet each dimension. In this manner, Table 4.1 and Table 4.2 present a selection of the most commonly used proxies for the Ghazalian fivefold taxonomy of *maqasid* (*see* the most recent related studies by: Ali and Hasan 2014;

[48] Malaysian government, in this manner, developed the 'Malaysian Syariah Index' as a benchmark to evaluate countries' performance in regards of fulfilling the objectives of Islamic principles.

Amiruddin 2014; Anto 2011; Batchelor 2013; Esen 2015; Kasri and Ahmed 2015; Mili 2014; Mukhtar, Nihal, Rauf, Wasti, and Qureshi 2014; Shaikh 2017).

The variables in the tables are chosen by many scholars of Islamic finance in an effort to best approximate the objectives of *Shari'ah* for different dimensions. The ultimate *maqasid* index, hence, would measure overall economic performance of countries with respect to its conformity to *Shari'ah*. In achieving this, some valuable indices have been developed including Islamicity Index (Askari and Mohammadkhan 2015; Askari and Rehman 2013), *Hayat-a-Tayyaba Index* (Mukhtar *et al.* 2014), Islamic Human Development Index (Anto 2011), *Maqasid al-Shari'ah* based Development Index (Ali and Hasan 2014), and Posterity Development Index (Khan, Sulaiman, and Bahari 2015).

Table 4.2: Variables for the Ghazalian Five-Level Dimensions

Hifz al-Din	Attendance in religious services Frequency in prayers/fasting Charitable giving and *Hajj* attendance Belief in God Avoidance from *Haram* activities
Hifz al- Nafs	Freedom of choice War or terrorist attacks Life satisfaction
Hifz al-Aql	High level of education Avoidance from alcohol consumption and drug use School attendance/achievements
Hifz al-Mal	Employability Income level / financial situation Savings and consumption Robbery and theft occurrences
Hifz al-Nasl	Frequency of sickness Access to health services Homosexuality and prostitution Abortion and divorce

Note: Developed from the primary data-based studies

Apart from country level performance based empirical studies, *maqasid* has also been employed for evaluating the performance of Islamic banks. In such studies, the wisdom and purpose behind financial activities are identified so that Islamic banks would observe them in their operations. However, constructing *maqasid* indicators alone is not enough; Islamic finance data must also be accessible and disclosed to evaluate Islamic banks' performances. One way of tackling this issue is to apply content analysis over the disclosed information in annual reports of Islamic banks. Mainly inspired from the distinguishing works of Islamicity Disclosure Index (Hameed *et al.* 2004) and Ethical Identity Index (Haniffa and Hudaib 2007), content analysis-based *maqasid* studies determine some key concepts for each indicator, and through using the method of codifying text and content, high frequency of reference to the statements assumes much importance for related indicators. Table 4.3 depicts a selection of widely used long-listed indicators of *maqasid* in disclosure studies (amongst others, *see*:Arshad, Ahmad, Fisol, Said, and Haji-Othman 2015; Asutay and Harningtyas 2015; Hurayra 2015; Ngalim and Ismail 2014). Despite giving a freedom of choice in determining variables, one of the disadvantages of disclosure studies lies in too much reliance on the disclosed information in reports. Besides, this evaluation method in fact checks *maqasid* scores of 'accounting reporting', not directly of Islamic banks' *maqasid* performance in reality or in the practical field; as non-disclosure does not imply that Islamic banks do not undertake such activities in their everydayness. Since disclosing information is a governance issue; and since such governance culture has not being consolidated in the Muslim countries, reliance on disclosed information to evaluate the *maqasid* performance may only provide a proximity to the reality. Lastly, it is very hard to reach a comprehensive performance measurement by using content analysis, since the validity and reliability will always remain questionable. Despite all these shortcomings, the contributions of Bedoui (2012), and Bedoui and Mansour (2015) is amongst the meritorious studies, which develops a conceptual measurement method for *maqasid* performances of Islamic financial institutions by extending and augmenting the concept of *maqasid* through introducing Abdel Majid Najjar's conceptualisation of extended *maqasid*. By adopting this structure, Asutay and Harningtyas (2015) conducted a content-based disclosure analysis and evaluated social performances of selected Islamic banks.

Table 4.3: Selected Variables Used in Disclosure Studies

Prohibition of *riba*
Opening *mudarabah* account
Provide *maslahah* for all
Microfinance activities
Profit and loss sharing
Employee education
Zakat and Charitable activities
Environmental responsibility
Good governance
Collaboration and sharing within bank staff

Another method of coping with data access problem is to conduct questionnaires and interviews and transform the assembled data into measurable variables through giving particular weights to each dimension (amongst the related studies, *see*: Mohamad, Ali, and Sharif 2016; Shaikh 2017). In doing so, interview method of data collection involves directing questions to scholars at *Shari'ah* supervisory boards, staff, managers and directors of Islamic banks. The results are interpreted with some *maqasid* benchmarks, and scores are given accordingly. Similar to content analysis, this method is also less reliable, since internal staff or scholars sitting at bank boards are most likely to provide pretentious answer by avoiding negative responses regarding Islamic bank's performances, which hence leads to response bias.

Lastly, *maqasid* index is also constructed through determining objectives of Islamic banking with some ratio analysis (*see*, for instance, Mohammed, Tarique, and Islam 2015; Nizam and Larbani 2017; Rusydiana and Al Parisi 2016; Shaikh 2017). Table 4.4 presents a set of widely used ratios that provide to assess *maqasid* performance of Islamic banks. As can be seen, it can be a terribly difficult task to correlate such items with the whole notion of *maqasid al-Shari'ah* as has been discussed so far.

Table 4.4: Selected Ratios for Assessing *Maqasid* Performance

Interest free income / Total income
Zakat distribution / Net assets
SME financing / Total investment
Training and research expenditures / Total assets
Employee retention ratio
Education grant / Total income
Profit / Total income
Investment deposit / Total deposit

Despite these attempts at constructing a *maqasid* index are appreciated as they provide some inferences about economic and financial performances, there are substantial problems inherent in developing these indices. First and foremost, it is debatable whether *Shari'ah* objectives within economic and financial sphere can be relegated to a limited number of dimensions. This question brings about another issue that concerns the validity of statistics as an adequate method to evaluate economic and social performance. As statistical methods require measurable forms of knowledge, the naturally immeasurable or unobservable factors are either declined or replaced with something different from the original (for a political economy approach towards the utilisation of statistical methods in social sciences, *see*: Bruno, Jany-Catrice, and Touchelay 2016; Desrosières 2002; Fioramonti 2014; Ziliak and McCloskey, 2008). Taking the example of the preservation of *al-'aql* as one of the primary *maqasid*, most performance indices relegate it to 'education'. In order to measure and quantify education, the existing data are sought and mostly 'education expenditure as percentage of GDP' or 'school enrolment' is chosen as they are readily accessible in the World Bank and other international databases. As a result, a particular country (can be economy or bank) is evaluated for its contribution to the preservation of *al-'aql* with such proxies of education; and if it gets high score, the country accepted as successful in conforming to the objectives of the *Shari'ah*. However, what happens in reality is nothing, but the quantitatively increased education opportunities or funds reserved for it. In the case that the education system is quite underdeveloped within a country, these proxies will contrarily imply biased results. More importantly, what al-Ghazali intends with this dimension of *maqasid* may not be equivalent to the proliferation of modern and positivist educational institutions as prevailing in the Muslim countries.

This study does not claim that *maqasid* index developers are all favouring such an approach; rather this is an inevitable route independent from subjective views once the need for measuring *maqasid* is taken for granted. If a particular dimension of *maqasid* is aimed to be measured, then there is no way other than to utilise the existing databases. Thus, even the best index that may be developed with appropriate components has to face the limitations imposed by mainstream databases. Considering also the data limitation of Muslim economies or even of Islamic banks, *maqasid* indices eventually cannot go beyond a symbolic meaning. Similarly, this approach results with falling in the trap of judging advanced countries more Islamic, for the performance results give higher ranks for developed countries as evidenced in the study by Askari and Mohammadkhan (2015). Although it does not mean that advanced countries are performing less from the Islamic point of view, it is like comparing the superiority of apples over oranges. In other words, the value-loaded dimensions of *maqasid* cannot be readily applied over different institutions emerged from different worldviews beyond shallow proxies developed from different ontologies. Therefore, if education is used for the *hifz al-aql*, the result would be the fact that a European country would always have the highest ranking, which indicates the 'unbearable lightness of the proxies' used.

In summarising the transformation of *maqasid* understanding and its application in Islamic finance throughout the decades, it can be stated that founding fathers' attempt of considering *maqasid al-Shari'ah* as the methodology for Islamic economics in defining its consequences has not paved the way for the emergence of an authentic financial system based on Islamic values and norms.

In light of the foregoing critical survey of the contributions made by the founding fathers of Islamic economics and those who came after them, the remaining sections of this study explores the question as to how *maqasid al-Shari'ah* can function as an essential methodology for Islamic economics. In doing so, problems pertaining to the adoption of al-Ghazali's *maqasid* framework and its use by Islamic finance scholars are addressed. Then, an attempt is made to bring to the fore the distinctive features and implications of a proactive *maqasid* framework in relation to Islamic economics.

4.5. *MAQASID AL-SHARI'AH*: TOWARDS AN ESSENTIAL 'METHODOLOGY'

Methodological issues have always been the moot point, particularly in economic theorisation, for they constitute the theory of knowledge or epistemological aspect of it. The methodology of economics, following the Western Enlightenment process, has mostly been developed around national interests, and the political economy of it evidences that such a methodology is subordinated to the legitimisation and theorisation of the real objectives of nation states.[49]

Methodology of (conventional) economics suggests that economic theory is part of the scientific knowledge and hence it must be verified by using empirical procedure in deriving objective facts and reason. Popper (1968), the main exponent in this area, entails empirical methods for validating economic theorisation through what he identifies 'falsification'[50] process. Together with much emphasis on empiricism, mainstream economic methodology also adopts the Darwinian principle of survival of the fittest in the market, *a priori* reasoning, utility maximization, and deriving economic theory 'from realities to doctrine' (Addas 2008:29).

In responding to the 'poverty of economics' resulting from scientific take up of neo-classical economics, and with the emergence of post-modernism, the scope of economic analysis has gone beyond the traditional borders of 'pure scientific' approach by also considering institutions, political economy, values, cultures and religious behaviour albeit as an exogenous variable. The emergence of institutional economics, new political economy and public choice, environmental economics among others heterogenous approaches, aim at expanding the horizon of economics by re-discovering the old wisdom of political economy by acknowledging the intersectionality of social sciences, which is also essential for Islamic economics, as it has always remained a moral and political economy in its broadest sense along with being 'sourced' from 'revealed knowledge' (Asutay 2018).

As regards to Islamic economics, with all these developments have been taking place in economics science, contenders in the field have not systematically pay attention to methodological issues in theorizing Islamic economics, yet they oscillated between two opposite poles: the 'step-by-step approach' and the 'all-or-nothing approach' (Hasan 1998) where the former approach exploits the IOK with a realist and pragmatist manner and believes an

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[49] For example, Adam Smith's seminal work on 'the Wealth of Nations', far from being universally suggestible to every nation, aims to investigate the ways that leads advanced countries in the Western world to the achievement of prosperity.

[50] The term 'falsification' is used, in methodological sense, that since truth can never be known, scientific progress must be maintained by falsification of economic propositions.

evolutionary construction of Islamic theory of economics thereto, and the latter approach – advocated mainly by Attas (1989) – necessitates the assumption of practicing Muslim society within its pure economic theory making, beyond evolving economics into Islamic framework as part of the *tawhidi* IOK paradigm developed by Faruqi. These two ramifications of methodological strategy pioneered in the literature, and *maqasid al-Shari'ah*, as mentioned above, is yet to burgeon to develop as a third alternative for the methodology of Islamic economics.

In light of the definition and function of methodology mentioned above, this study, beyond the two oscillations, suggests recourse to *maqasid al-Shari'ah* as the fundamental methodology for the theorisation of Islamic economics through which Islamic developmentalism can be conceptualised and transformed into public policy making. When methodology is adjusted to the ambit of Islamic economics, *maqasid* functions to explain:

(i) the way that the sources and origins of knowledge, that is primarily *Qur'an* and *Sunnah*, is articulated into the base of its economic theorisation;
(ii) the way that the Islamic axiomatic approach is substantiated and instituted to articulate these sources into everyday socioeconomic life,
(iii) the way that the Islamicity of the institutional and non-institutional forms of these articulations are verified in both intentionalist and consequentialist manners.

To further elaborate on these two approaches, owing to the intentionalist adoption, *maqasid* can provide theoretical, philosophical and also practical reference point to develop socioeconomic policies. Consequentialist approach, on the other hand, functions to identify morally acceptable outcomes among others, which, hence provides a methodological framework to measure the policy outcomes in relation to intentionally established *maqasid* scheme. Despite the fact that consequentialism or substantivism has traditionally been ruled out as part of methodology in Islamic economics by the proponents of *fiqhi* approach due to the adoption of 'intentionalist' or form approach, this study suggests that *tawhid* in the form of complementarity leading to unitarity necessitates 'intention' and 'consequence' to be considered together as part of the methodology of IME (Asutay 2018).

Adhering to this conception, together with the intentionalist and consequentialist approaches, *maqasid* can embed its distinctive epistemological spirit and methodological characteristics into economic system in such a way that the role of 'individual faculty, reason and rationality' in deriving knowledge, 'self-interest and utility maximization motives' in shaping economic behaviour in line with *homoeconomicus*, 'market exchange and price mechanism' in establishing justice and equity through allocation of resources, and 'the harsh competition and craving for efficiency' as the overall *modus operandi* are all examined critically, as these have influenced

Islamic economics and finance theory and practice. Instead, the revealed knowledge as the source of epistemological knowledge, *falah* (salvation), *ihsan* (beneficence), altruism, and cooperative and sharing behaviour through expanded stakeholding understanding, substantive morality beyond instrumental reasoning, efficiency with equity, and ethico-economic relationship within Islamic order are located into the construction of authentic Islamic theory of *iqtisad* (Islamic economics) or IME through the methodology of *maqasid al-Shari'ah*. At the end of this process, it is expected that *maqasid* embedded Islamic theory of *iqtisad* should generate a particular social formation that is distinct from capitalist social formation and capitalist modes of production, as *tawhidi* governance mechanism suggests an extended stake holding and the interests of all stakeholders are considered equal. Hence, this process should lead to *ihsani* or 'good society' as opposed to capitalist commercial society.

This study, accordingly, reconsiders *maqasid al-Shari'ah* to constitute the fundamental methodology in respect of Islamic developmentalism that encompasses the entire process through which knowledge relating to economic phenomena is authenticated. This can, in turn, lead to establish a substantive IME understanding wherein interpersonal and social relations are not merely relegated to economic relations, but economic system is embedded into norms and values of society through locating ethico-economic relationship across each system so that morality can be articulated beyond impersonal market environment.

4.5.1. Re-embedding *Maqasid al-Shari'ah* into the Theory of Development

As has been shown in the survey of the relevant literature in the preceding section, the existing contributions on theoretical construction of Islamic economics limitedly dealt with the notion of *maqasid al-Shari'ah* and its essential role in constituting a fundamental methodology. However later, ironically, *maqasid* has been accommodated into Islamic finance, which is one of the institutional constructs of Islamic economics, such that the Islamic financial transactions and the operations of IBF institutions have implicitly been legitimised through *maqasid*. In addition, *maqasid* has also been used by the critics of Islamic finance to identify its social failures. For example, financialisation of Islamic finance today, increasingly switching into the orbit of global financial gear, is being evaluated positively through various *maqasid* indices developed by contemporary empirical studies based on econometrics method.

The rationale for the exclusive interaction of *maqasid* with Islamic economics in such a way mainly stems from the pursuit of recalling the well-formulated objectives in the Islamic intellectual history in today's environment, especially after recognising the failure of Islamic finance project due to its mimicry of conventional finance. Thus, it is believed that severe criticisms raised against Islamic finance could be obviated through a re-examination process over IBF applications by introducing *maqasid al-Shari'ah*[51]. Accordingly, since al-Ghazali's *maqasid* framework was ready to be adopted, *Shari'ah* scholars at *Shari'ah* boards of IBF institutions used this particular frame to legitimise their product regardless of its divergence from the ideal position. This study, nevertheless, suggests that the Ghazalian approach to *maqasid* in producing an ideal methodology for Islamic economics is inadequate on the grounds of its inherent flaws in revealing developmentalism as identified above.

Deficiencies in the Ghazalian framework with respect to its methodological functionality can be identified and explored under two main points. The first one, 'individual orientedness' (*fardiyyah*), is characterised by lacking explicit emphasis on societal aspects within each objective. For instance; the objectives determined through preservation of faith, soul, wealth, mind, offspring (and honour) all embraces individual preference, perspective and scope, hence the derivation of social consequences from these individually expressed five essentials is not plausible as the social dimension must be embedded in *maqasid al-Shari'ah per se* beyond instrumental or indirect ways. Indeed, the argument that the satisfaction of individual needs would, in return, lead to prosperity in societal level is an arguable method in many aspects. In theorising the capitalist system, Adam Smith (1976) [originally published in 1776] had adopted a similar method, which can be termed as handicap of individuality, albeit the objectified consequences are in great contrast to Islamic premises, by claiming that the 'invisible hand' would establish social welfare and prosperity and lead to society's opulence so long as every single individual seeks the pursuit of his own gains in line with self-interest motives. In other words, Smith (1976) argued for a virtuous society in which prosperity and wealth can only be established in societal level by setting some goals that confine its scope to individual. This inductive method, however far from Smith's expectations, has not benefited society at large as the scattered history of capitalist development evidences.

It is a methodological problem, hence, that the mere consideration of individual *falah* does not necessarily bring out social justice, welfare, and developmentalism; thereby *ihsan* (beneficence) as a societal objective should be conflated with individual level *falah* (salvation) so that behavioural attitudes can be moulded by these two elements in order to reflect upon norms and values of society. In other words, societal objectives can be fulfilled through

[51] The eclectic approach upon the establishment of *maqasid* into Islamic economics realm is exemplified in the previous sections, which surveyed the emerging literature on Islamic finance and *maqasid*. Thus, particular reference is not rendered here.

enhancing *falah* aiming to expand *ihsani* social capital. It can, therefore, be argued that the rationale for stressing on individual centricity in developing Ghazalian *maqasid* emanates from the fundamental exigency of developing and expanding the capacity and functioning of individual. However, notwithstanding the greatness of the ultimate objective, *tawhidi* understanding of Islam essentialises the concept of *ihsan* in the process of fulfilling this fundamental objective so that each individual's capacity and functioning would harmonically contribute to the wellbeing of others. Consequently, such a process invalidates the individually acceptable but socially defective objectives and outcomes (or *vice versa*) through its *tawhidi* framework, which functions to set objectives in a harmonious and complementary way. Thus, eventually, human beings pursue *falah* as part of their objectives, on the one hand, but they also increase *ihsan* amongst their fellow citizens to establish socioeconomic justice and equity in this world and to reach eternal happiness in the hereafter, as the two-dimensional utility function of Islam suggests (Asutay 2007b, 2012). In other words, as Naqvi (1994) identifies, *ihsan* should be considered as an 'equilibrium' in the sense that those individuals reaching their *falah* should consider the *falah* of others through doing and expanding *ihsan* and hence bringing up other less-fortunate ones in the steps of *falah* ladders.

Another deficiency is 'the lack of proactivity' which becomes obvious with such words of 'safeguarding', 'preservation', 'prevention' and 'protection'; all referring to what al-Ghazali uses as '*hifz*'. Thus, *hifz* evokes a closed system of objectives that is far from being dynamic in nature and hence unable to be adaptive with and moulder of changing circumstances nor can it help to produce public policy as a consequence. However, as a counter argument to this statement, Chapra (2008:5) advocates:

> if we wish also to ensure the sustained development and well-being of a society, the word 'safeguarding' used by al-Ghazali […] need not necessarily be taken to imply preservation of just the status quo with respect to the realization of the *maqasid*. We safeguard when we have reached the peak of achievement. However, this is not possible for human beings in this world. There is always room for improvement. The verdict of history is that unless there is a continuous progress in their realization through a movement in the positive direction, it may not be possible to safeguard them and to sustain the society's well-being in the long-run. Stagnation will ultimately set in and lead to decline.

As can be seen, Chapra (2008) supposes 'safeguarding' to be realised when the 'peak of achievement' is reached. However, since the peak is not reachable in this world, there should always be continuous search for, and pursuit of, betterment. Chapra (2008), thus, aims with this statement to bring back the dynamic structure of *maqasid* under *hifz*. This approach, albeit quite optimistic, impels the limits of the concept of safeguarding that is why he prefers using 'invigoration' (Chapra 2008:8) in *lieu of* this concept.

As regards to the 'prevention orientedness' being a problematic approach, 'proactivity' transcends aforementioned prevention based *hifzi* approach and its variants in the contemporary era and sustains its authenticity and vividness in every time and place without any stagnation. The proactive *maqasid*, in this sense, echoes Mawlana Jalal-el-din Rumi's (1207-1273) 'metaphor of drawing compass' (Akman 2017) according to which one leg of the compass holds still and rooted in a certain spot statically and the other leg arcs the entire surface without causing any translocation in the former part. By making use of this metaphor, proactive *maqasid* framework, in the same vein, takes nourishments from the entire historical intellectual pool by utilising numerous philosophical contributions, *ijtihads* and theories, and concurrently reforms and keeps alive itself without any disengagement from the ontological foundations of Islam. Nevertheless, if the former leg trends multiple shifts from the original spot towards others, then there will be plenty of circles drawn, which, in turn, reveal multiple intersection sets. In customising to *maqasid al-Shari'ah*, consequently, the intersection sets hold a composite of various epistemological knowledge articulations derived from different ontologies. As a result, there will be a hybrid *maqasid* understanding that is far from being authentic and distinct.

Rejecting the static and reductionist understanding of *maqasid,* Ibn al-Qayyim explains the spirit of proactive *maqasid* through his identification of *Shari'ah* in the following momentous words (taken from Auda 2007:xxi):

> The *Shari'ah* is based on wisdom and achieving people's welfare in this life and the afterlife. *Shari'ah* is all about justice, mercy, wisdom, and good. Thus, any ruling that replaces justice with injustice, mercy with its opposite, common good with mischief, or wisdom with nonsense, is a ruling that does not belong to the *Shari'ah*, even if it is claimed to be so according to some interpretation.

In line with this elucidation, *maqasid* as the essential methodology of Islamic economics should be imbibed and moulded by the moral principles and values discussed above in order to sustain its proactive nature and applicability down the ages.

While the two main deficiencies, *fardiyyah* and the lack of proactivity, should be dealt through the lens of proactive *maqasid* understanding, it should also be acknowledged that modern critiques to al-Ghazali claiming lack of universal objectives in his *maqasid* framework such as justice and freedom (Al-Ghazali 1996), socioeconomic reform, women rights, and abolishing slavery (Ibrahim 2006), research and development (Kamali 2008), environment and poverty alleviation mostly overlook current inclusion of these elements into Ghazalian *maqasid* as absorbed and permeated through the theoretical foundations of his *maqasid* insight. Leaving aside the notion of justice that saliently connotes social dimension, other notions are, to a large extent, gathered into *maqasid* discourse by some reformist Muslim scholars with the aim of universalising the modern problems of Western world. This is a major fallacy in terms of being adaptive and responsive such that specific problems that appeared in different formations of societies in the same timeframe has been transmitted into Muslim intellectual world with the same context and form.

The concern is to judge predecessor Muslim scholars, with anachronistic reasoning, as if they neglected or omitted such imported issues in their theorisation. To give an example, environmental concerns from public policy aspect, when compared to the embracement of the term in the modern period, has not been emphasised in such a manner during the intellectual debates in the Muslim history, since both Muslim governors and philosophers dealt with the protection of environment under the broader theme of socioeconomic justice and equity. When environmental problems emerged in a particular society, then it used to be considered under the more general objective of establishing justice for future generations, as *adl* or justice relates to inter-and intra-generational justice (Naqvi 1994). Thus, coming back to the main debate, 'thinking beyond the box' entails an approach that transcends the ambit of conjectural considerations of *maqasidi* thinking; thereby *maqasid* has to be cleared from politically or economically biased conjectural and expediential expositions. However, it does not mean that such issues, which are free from bias, would not be located and evaluated within *maqasid* framework.

Besides the two main deficiencies in al-Ghazali's *maqasid* frame itself and the reformist Muslim scholars' misinterpretation of the overall Ghazalian *maqasid* framework, hedging *maqasid* around the essential levels of traditional classification is another problematic that must be avoided. *Ihsan*, here, as this study essentialises, has a great impact on all three levels of necessities to realise *maqasid* in every sphere of life. Instead of hierarchically classifying *maqasid* as essentials (*daruriyyat*), exigencies or complementary (*hajiyyat*), and embellishments (*tahsiniyyat*), it should be considered as the complete process at the end of which real and eternal happiness is achieved in both individual and societal level, as Islamic process relates to 'becoming process'[52] permeates around ongoing development in every aspect including *ihsan*-oriented development, as Chapra (2008) suggests that reaching perfection is not possible in this world and therefore there always exists an 'ongoing room for development'. Through this, *ihsan* makes everything embellished, as the term connotes, and this everlasting embellishment process is nestled, instituted and expanded across the society and does not stop with any satisfaction or fulfilment of basic needs.

Islamic economics, in vitalising embellishment, should aim at developing structures to advance the degree of *ihsan* in every step of individual interaction with his surroundings (with other individuals,

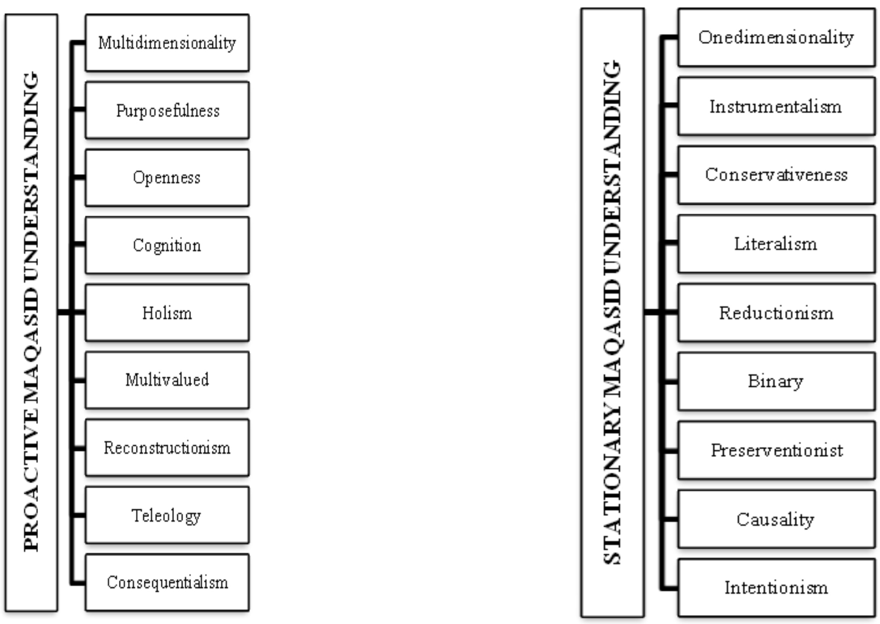
[52] See the debate on 'becoming process', Jing and de Ven (2016).

environment, animals, machines, *etc*.). For instance, the invention of coffee machines that take place in every workplace all over the world is quite functional in terms of making life easier especially for those who always rush for their jobs or businesses. However, beyond being functional and efficient, the *ihsani* approach also essentialises the existence of embellishment and aestheticism in every sphere through making things 'life-enhancing'. In this manner, the famous Japanese tea ceremony reflected the aesthetic and life-enhancing nature of Japanese culture, which coheres with the *ihsan*-based perspective. Likewise, the articulation of *maqasid* oriented thinking into institutional forms has to be expanded and scattered to the three levels of necessities in a holistic way without strict lines thereto, and transitivity of each level should be yielded easily within *ihsan* approach so that the ultimate objective can be achieved in an interacted manner. This will fit into the *tawhidi* methodology's unitarity and complementarity expectation, as all these three level will be considered simultaneously important.

4.5.2. Distinctive Features of the Proactive *Maqasid* Framework

Based on the fundamental principle of proactivity, which entails an embedded and all-embracing character in identifying and implementing the *Shari'ah* objectives, *maqasid al-Shari'ah* as a discourse embraces some distinctive features through which authenticity, vividness and dynamism of Islamic developmentalism is realised. Owing to the systems approach, these distinct features can be demonstrated, together with comparing that of the stationary *maqasid* understanding, as in Figure 4.1:

Figure 4.1: Proactive *vs*. Stationary *Maqasid al-Shari'ah*



As can be seen in Figure 4.1, each feature demarcates and sheds light on the scope and substance of the proactive *maqasid* framework. In doing so, complementarity between each feature provides interdependency such that the scantiness of some features in the framework fades the strength of *maqasid*. Multidimensionality, in this sense, requires the existence of holistic, multivalued and reconstructionist characters to function smoothly, as opposed to the poorness of one-dimensional explanations. Therefore, in the *maqasid* realm, it entails conflating the level of necessities, scope of the rulings and the level of universality simultaneously in its framework. In other words, the proactive *maqasid* approach should reflect the traditional classification characterised by an *ihsan* spirit and orientation as explained above and expand its scope to societal levels by eliminating the shortcoming posed by individuality, and also should capture universal objectives through which particular and specific *maqasid* can be derived.

This perspective, explained with multidimensionality, requires expanding the horizon of *maqasidi* thinking by questing for different approaches and suggests pondering upon the possibility of more than one *maqsid* that are inherent in the related epistemological source. However, the general tendency in internalising *maqasid* into Islamic economics is towards adopting single evidence for the addressed issue by using *maslahah* in unsophisticated and pragmatic manner. By the same token, the binary character of the orthodox stationary *maqasid* understanding of contemporary times compels choosing between two contrasting alternatives, which are mostly the opposite far ends of two edges, such as *fard* (mandatory)/*haram* (unlawful), *sahih* (authentic)/*fasid* (invalid), *salafi* (traditionalist)/modernist, conservative/reformist and so on. However, multivalued aspect urges to go beyond the zero-sum logic or black/white approach by introducing some intermediate categories that bring flexibility and transitivity in realising *maqasid*. This problem, meanwhile, is not seen in the history of Islamic law since scholars in those periods introduced intermediate categories and developed authentic views by adopting multivalued dimension. In the case of IBF, *maqasid al-Shari'ah* should likewise consider financial operations by introducing multi-filters amongst which the compliance to the *fiqhi* rulings, namely negative screening, constitutes only one aspect. Ideally, one would expect to achieve this goal more likely in today's post-modern world since deconstructionist adoption of post-modernism would reveal multivalued character in IBF; nevertheless, these approaches, when applied to Islamic law, still tend to content with one-dimensional and reductionist explanations. As a result, moral objectives within IBF are mostly neglected or mentioned in an eclectic way at best; therefore, compliancy process should also consider positive screening by examining and internalising the consequences in the decision-making process in terms of achieving substantive morality.

It is an overwhelming fact that deconstructionist approaches to Islamic law applied by post-modernist Islamic scholars, contrary to the expectations, have deepened the divergence between *fiqh* and morality. More precisely, in search for *maqasid* of the rulings and past evidences, knowledge has been deconstructed in a right manner to crystalize the objectives, but deconstructed knowledge was decoupled from the original whole permanently and reconstructive stage has never been reached, as it was before witnessing or experiencing the process of disciplinisation of knowledge. However, the basic rationale for deconstructing knowledge is to grasp the unseen at first sight in the whole picture with the aim of reconstructing it at the end lest it deviates from the original. Realising *maqasid*, in the same vein, essentialises the complete process of deconstruction and reconstruction, as epitomized with the metaphor of drawing compass.

In order to make the entire process of deconstruction and reconstruction acting in concert, holistic dimension plays an important role here – remembering the complementarity nature of each feature emerged from *tawhid* – since it reminds the very basic idea that deconstructed and disentangled segments cannot display the whole picture in their own right, but these segments rather give important expressions and understanding about it. Reductionist/partial or atomistic approach to Islamic law, in this sense, neglects the holistic dimension of *maqasid al-Shari'ah*, hence, it can never explain and link partial objective within the main objective due to relegating the entire process of deriving *maqasid* to the partial one.

The idea of establishing IBF sector, in the same vein, should be considered under the holistic objective defined by Islamic economics. In other words, holistic approach explains IBF as an important component of Islamic economics that contributes to the realisation of the ultimate objectives of *falah* and *ihsan*, whereas reductionist approach treats IBF as a self-appointed and dis-located field that has its own objectives, which are subject to alter with the changing circumstances and not necessarily connected with the ultimate objectives. One of the reflections of the latter approach implicitly suggests dealing with IBF as an isolated field, which does not necessarily aim to realise social objectives, but rather has its own financial objectives such as the everlasting passion to grow its assets and operations and exhibiting similar functions with conventional banking through being an important part of the global financial sector.

As one of the essential features of proactive *maqasid* framework, purposefulness stands against the liberal notion of instrumentalism, as *maqasid al-Shari'ah* itself evokes a purposeful character beyond attaching an instrumental role to each dealing separately. Therefore, every step in fulfilling a particular objective creates interdependent purposes, in a holistic way, complementing one another, without considering any of them as an instrumental part. In articulating purposefulness into Islamic economics, it is essential to accommodate 'substantive morality' at the core of its theorisation, for the moral dimension must be embedded by its very nature of being a value-loaded system aiming to fulfil a particular objective. However, beyond purposefulness, instrumental approach to morality breeds the notion of 'instrumental morality', which basically functions to deal with things through instrumenting and eroding their essence. A good example of instrumental approach to moral dimension in Islamic economics can be given by the role of *Shari'ah* experts in IBF field. Accordingly, moral issues are considered only to be an instrument in the hands of *Shari'ah* experts who can decide on behalf of IBF customers about the compliance of a contract to the principles of divine knowledge.

The purposefulness feature of *maqasid al-Shari'ah* accompanies with the tension between openness and conservativeness in approaching contemporary socioeconomic problems. As Muslim intellectuals face the challenges of establishing an authentic Muslim identity with its full characteristics in the postmodern world, two alternatives surface as a response to this situation. One of them is adopting a conservative approach while confronted with modern scientific knowledge and its secular institutions. This approach is unable to construct the Muslim worldview in contemporary times, but rather it yearns for the same social formation in prophetic times to prevail again in the modern world. The openness approach, however, recognizes existing conditions of Muslim world and aims to harmonise Islamic thought by proposing new ideas and establishing authentic institutions. In doing so, it adopts the aforementioned metaphor of drawing compass. Forming an authentic *maqasid* framework, hence, necessitates the inclusion of openness character in order to get rid of anachronistic expectations from the romanticised history and to allow for a dynamic and proactive thinking.

One of the aspects of conservatist approach is related to literalist or textualist interpretations of divine sources, which limits the boundaries of *maqasid* provisioning and undermines the burgeoning of *ijtihad* process therein. As contrast to literalism, *maqasid al-Shari'ah* vitalises cognitive aspects of Islamic law by suggesting a distinction between revealed knowledge and its cognitive part that allows for re-functionalising *ijtihad* mechanism in contemporary times.

A teleology-causality debate reflects another important aspect of proactive *maqasid al-Shari'ah* framework. As mentioned before, modern scientific thinking experienced a serious shift from teleology to causality through the essentialisation of causal reasoning by introducing the cause-and-effect dialect which entails causality as the central logic of thinking. Thus, teleological adoption in any theory was regarded as metaphysical and hence completely rejected.

By acknowledging the distortions of causal positioning, *maqasid al-Shari'ah* suggests recourse to teleology by embedding 'theologically' defined developmentalist objectives. In this respect, modern scientific methodology that entails causal way of thinking has to be replaced with teleology, which explains a phenomenon with the function of its 'purpose'.

Lastly, proactivity suggests that the intentionalist limits of presenting *maqasid* conceptions can be overcome by introducing consequentialism. More precisely, intentionalist and consequentialist crosschecking simultaneously determines the framework of *maqasid* through establishing harmony between them as suggested by *tawhidi* methodological frame. In the case of IBF, the observed mimicry and hybridisation adopted by Islamic finance can be overcome whereby authenticity can be achieved through this crosschecking system, since form-based interpretation and evaluation of the practices of Islamic finance cannot go beyond intentionalist limits and fails once the consequentialist checking is applied.

4.6. EMBEDDING *MAQASID AL-SHARI'AH* IN ISLAMIC FINANCE DECISION MAKING: AN ATTEMPT

The discussion so far essentialises the importance of embedding *maqasid al-Shari'ah* into Islamic economics and finance decisions to yield a substantive morality-oriented outcome. This idea is expressed and articulated in Figure 4.2.

As can be seen in Figure 4.2, IBF responds to the financing and banking needs of their Muslim customers through the available Islamic financing contracts. *Shari'ah* compliancy of products and the Islamic legitimacy of contracts are ensured by the Islamic sources in the form of *Qur'an*, *Sunnah*, *Ijma*, *Qiyas* and *etc*. IBF solutions are produced through such a *Shari'ah* filtering mechanism and the solution as part of the negative screening process has to fulfil the conditions or requirements of the *Shari'ah* compliancy process, which are identified in purple boxes in Figure 4.2.

As the practice of IBF so far demonstrates, such an 'intention' oriented process is relegated to negative screening. However, *maqasid al-Shari'ah* does not consider 'harm' and 'unlawful' to be sufficient criterion; thereby, it suggests that positive consequences should be produced in a proactive and dynamic manner to yield an outcome which can essentialise social and human development as well as economic development. Therefore, requirements have to reflect such positive screening to endogenise IME compliance through evaluating the consequences of the process with the objective of ensuring that the consequence is 'morally *Shari'ah* compliant' beyond *fiqhi* compliance. In other words, the 'green' box in the right-hand side bottom corner of Figure 4.2 should be considered as a substantivist condition in the form of moral and developmentalist requirement. In order to produce morally acceptable 'consequences' through endogenising or embedding process of left-hand side green box, there is a need for moral screening process along with *fiqhi* screening process. Therefore, product development and operations related decisions at the IBF has to endogenise the green box located at the top right hand-side of Figure 4.2 as part of the larger *Shari'ah* compliance beyond *fiqhi* compliance. This will ensure *tawhidi* methodology of intention and consequences to complement each other to yield unitarity and a full *Shari'ah* compliance.

The product development process in the Islamic finance industry, if pursued by applying positive and negative screening processes under *fiqhi* and moral expectations, should respond to and override form-substance, or *Shari'ah*-compliant *vs. Shari'ah*-based debates (*see*: Abbas 2015). However, in practice, the endogenisation of moral screening into the newly developed Islamic financial products is never questioned due to the common belief that '*fiqh* by definition embraces morality'. The counter argument and evidence can be simply asserted here that morality may not be embedded in the process even though *fiqhi* requirements are fulfilled, as some forms of *sukuk*, *tawarruq* and *murabahah* financing bring the moral failure to the light. To further reflect on this, we can think of an Islamic bank, which had previously been operated as conventional bank and well-appreciated with its agricultural financing. However, later, it has expanded its operation as commercial bank not limited itself in agricultural finance until its transformation into Islamic bank. A farmer, who produces wheat in his land, comes to this Islamic bank and askes for *salam* contract. The bank rejects him due mainly to the potential risks embedded in the *salam* contract and the profitability of other forms of contracts that are relatively less risky. The farmer, then, has to go to a conventional bank unwillingly and ask for interest-based loan as they do not have any alternative financing option. After the credit is used for bearing the costs including the cultivation of land and buying the seed, the farmer harvests the crops and sells them in the market. Then, the farmer gets money and initially pays back the credit with its interest. The rest of money in his hand, then, is deposited in the deposit account in the Islamic bank that rejected his application for *salam* contract-based financing. Not limited with this, other farmers follow the same process with the Islamic bank. Such accumulated deposits of these farmers in the Islamic bank, then is pooled in its main branches in big cities and used in minimum risky financial contracts such as *murabahah*, *tawarruq* and *sukuk* with bigger businesses or consumer durables financing.

The entire process, in consequence, has no objections with *Shari'ah* compliancy, but stands at odds with moral screening, as it is expected that an agricultural oriented Islamic bank should serve the financing needs of its main constituents, namely the farmers. While the farmers' main financing expectation is not fulfilled, their deposits in their Islamic bank are then used to finance bigger and larger businesses resulting into a transfer of economic power in the interest of the wealthier despite the farmers religiously oriented behaviour. This example evidences how Islamic banks can produce morally deficient outcomes by conforming to Islamic legal requirements. Thus, the developed *maqasid al-Shari'ah* framework is essential for Islamic financial decision making.

Based on these experiences, the model developed in Figure 4.2 suggests a reconsideration of the existing pattern applied not just product development but also the established institutions together with their working system. Accordingly, it goes beyond stationary perspectives on enhancing Islamic financial area and develops a proactive *maqasidi* framework to be applied for the theory making of Islamic economics and practical implications of Islamic finance on the basis of removing *fiqh*-morality dilemma by suggesting morally driven and *fiqhi* compliant knowledge articulations.

The historical origins of such a decision-making process rendered in Figure 4.2 can be found in various institutional examples in the Muslim lands in different eras of history. The institutions of *hisbah* and *ahilik*, for instance, were established to address particular needs of society with the harmonisation of morality and *fiqh*. *Hisbah* institution, in this manner, takes account of intentionist and consequentialist implications of market system; thereby, market is regulated to forestall unjust operations, which may cause monopolistic or oligopolistic power structures within market system. Therefore, the *Shari'ah* filtering mechanism, there, was applied to produce and ensure social justice in the overall economy and society.

The attempt with the depiction of Figure 4.2, in brief, aims to recall the old wisdom of *maqasid*-based knowledge creation methodology that should be applied in the entire economic system including financial sphere so that social justice expands and can be articulated into societal and economic institutions in an embedded manner.

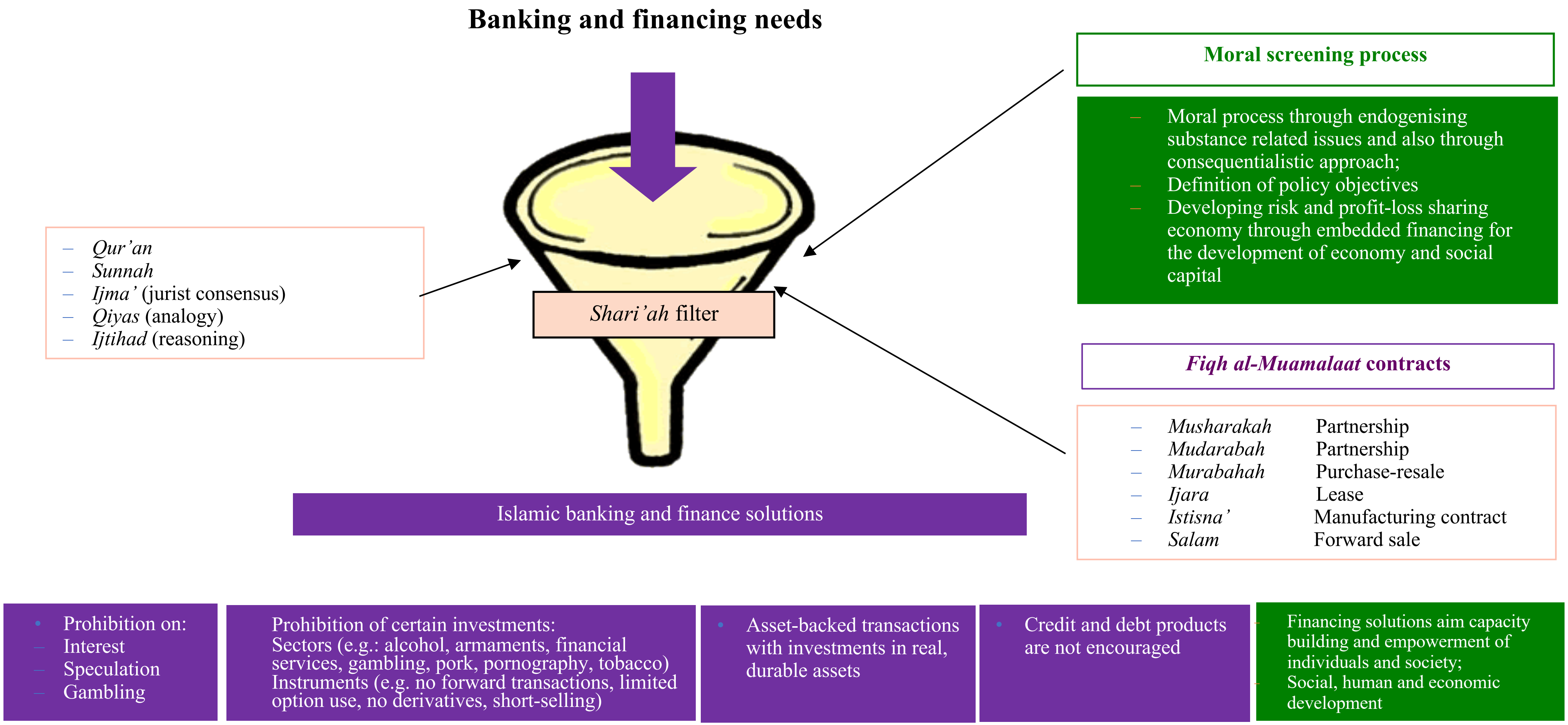
4.7. CONCLUSION

Establishing authentic institutions to redesign prevailing social formation of a society is not a fledgling phenomenon peculiar to post-modern era. Contrarily, every society somehow has faced the challenge of finding out the ways to embed shared norms, values and principles into its social, economic and political institutions. The idea of Islamic economics is such an attempt that was emerged in the post-modern atmosphere with an aim of establishing economic institutions, which are subordinated to the whole objective of achieving a good life (*hayat tayyibah*) from an Islamic perspective (Arif 1985). Succeeded or not, the experience with and discussions under Islamic economics and finance ascertained that the initial concern with theory making should be on methodological issues, for knowledge can only be authenticated through a rigorous methodology, which has been the main underlying shortcomings of Islamic economics and finance related studies and practices.

In search for addressing methodological dimension, despite being mentioned often in everyday practice, *maqasid al-Shari'ah* has almost been neglected beyond paying 'lip-service' in Islamic economics and finance literature, although it has great potential to function as an essential methodology. Instead, it was made subservient to a justification mechanism maintained with Islamic finance sector. Controversial and disputable issues within the sector have been resolved through a symbolical use of *maqasid* and *maslahah*, thereby Islamic finance has displayed a smooth parallel with mainstream financial progress. It is not surprising, in this regard, that *maqasid* perceptions of governments, *Shari'ah* scholars and some academics favouring self-regulated market economy system are all homogenous through the prevailing form-based understanding with the neglect of substance. Therefore, an economic system which is conceived to reflect Islamic notions but in fact not much different than capitalist framework can only reveal a form-based understanding bounded with methodological individualism, and hence fails to go beyond concerning utility maximisation, essentialisation of price mechanism, market exchange and efficient use of resources. However, proactive *maqasid* understanding removes such a dilemma by channelling both form and substance in the service of social good in a harmonious way.

With the recognition of failed attempts of instrumentality and eclecticism in *maqasid*, it is of special importance that theoretical grounds of Islamic economics should be re-examined in light of the proactive *maqasid al-Shari'ah* framework with its dimensions expanding the horizons of established understanding. In doing so, the flourishing of Islamic developmentalism in post-colonial Muslim nations would have been possible, since proactive *maqasid* envisages a totally

Figure 4.2: The Decision-Making Process in Islamic Banking and Finance



Source: Asutay (2018)

endogenised methodology and approach towards developmentalist considerations when compared to existing applications of *maqasid* based on methodological individualism.

Morality plays a pivotal role on the entire process of knowledge authentication through *maqasid al-Shari'ah*, while the current use of *maqasid* in IBF demonstrates that it has been relegated to *fiqhi* injunctions and used as an instrument to legalise particular product and operation in a legalistically rational manner. This runs against the expectation that *maqasid al-Shari'ah* should constitute the essential base of methodology for IME, as deductive reasoning based on Islamic ontology and also historical practice suggests that we should constitute IME beyond the narrowly defined Islamic economics as latter refers to *fiqh,* while the former is constituted through essential and pro-active *maqasid*. Thus, substantive morality should be embedded through *maqasid* in the theoretical underpinnings of Islamic economics to generate IME to fit into *maqasid* expectations as a distinct system of economics, so that *maqasid* objective of 'whatever is done should be essentialising and in accordance with human well-being' can be achieved. This requires interpersonal and social relations not to be merely relegated to economic relations, but economics and finance should be embedded by the norms and values of society through locating ethico-economic relationship across each system so that morality would be articulated beyond impersonal market environment. Thus, *maqasid* or essentialisation of human well-being in economic and financial activities takes place by motivating economic forces for economic, social and human development, which constitutes a base for the articulations of economic and financial choices to be linked to their 'consequences' beyond mere 'intentions'.

CHAPTER 5

CONCLUSION AND DISCUSSION: AN INTERPRETATIVE ATTEMPT

5. 1. SUMMARY

The idea of Islamic economics emerged and developed as a response to post-colonial redesign of world political economy with the objective of constructing an authentic economic system based on Islamic values system and normative world. It is expected that such a paradigm would extinguish inferior situation of Muslim world and pave the way for social and economic development. The emphasis on the notion of development stems from the fact that Islamic economics has always envisaged establishing social justice and social good through developmentalist perspective. Thus, by nature, it should generate development-based policies and institutions. Nevertheless, it is hard to claim that Islamic economics has successfully articulated developmentalism during the last few decades and hence failed to become an ambitious alternative to mainstream economic understanding by achieving paradigmatic change through its ontological and epistemological distinctiveness.

Considering the historical experience with the diffusion and expansion of Islamic finance, this study aimed at gaining a new insight on the idea of Islamic economics, its development throughout the last few decades and challenges in realising its aspirations. For this, first, it was important to revisit and examine developmentalist promises of Islamic economics, which was one of the main thrusts in the emergence phase, and the extent of its implementation in the policy level. By doing so, it is possible to see the extend by which the practices diverged from the developmentalist aspirations.

Acknowledging that Islamic finance is the sole institutional articulation emerged from the theoretical base, empirical evaluation of Islamic banks' performances is a meaningful attempt to examine the divergence. As we assume, the divergence is serious and leads to observed social and developmentalist failure, in the second stage, it is worth to shed light on the failure of Islamic finance project from the perspective of financialisation, since the failure roots in, to a large extent, the adopted 'financial logic' borrowed from mainstream economics whereby the utmost importance is given to financial sector to take place and substantialise at the core of economic activities. Lastly, this study argued that developmentalist failure and the resulting financialisation mainly stem from the lack of a proactive methodology that can be applied over theorisation of Islamic economics. It is therefore suggested that *maqasid al-Shari'ah* must be incorporated into the theory making of Islamic economics as a proactive methodology so that Islamic finance and banking practice can also articulate such values and outcomes.

5.2. WHITHERING AWAY ISLAMIC FINANCE OR A NEW FORM BASED ON OLD NORMS: A DISCURSIVE DISCUSSION

The entire debate on the relationship between finance and growth –together with the contributions of empirical studies aiming to explore the nature of this nexus- has dramatically shown up two important inferences as to how Western economic orthodoxy approaches human wellbeing, growth and development issues particularly in a world where finance is drastically being disembedded from economy and from the objectives of society. The first inference pertains to the incontestable prevalence of the concept of growth against development in the whole theoretical discussions and empirical studies such that almost every discursive study and quantitatively empirical research refer to growth in order to elucidate the impact of finance-related institutional and non-institutional effects on individual, society and economy.

In a similar vein, the second inference urges upon the evolvement of economies into a heavy financialisation pattern, which necessarily accompanies with a substantial change in the goal of economic activities. This approach argues that finance is no longer considered to be a tool for improving individual's capabilities and functions through enhancing economic performance, but rather the aim with financialisation process is to employ an opportunity space, independent from the objectives above, where various incumbents, pressure groups and rent seekers aim to financiate and commodificate values and 'things' through various financial institutions (multinational companies, stock markets, banks and *etc*.) and instruments, thereby these can be sold in the market as a commodity which allows for the interest groups to make private gains from them.

Through comprehension of the great divergence between economy and finance, it becomes more understandable why financial development and its impacts on socioeconomic life are narrowly dealt, by mainstream economists with such indicators of capital, savings, investment, technology and so on. These indicators incommensurately show one side of the coin, which explains finance-based economic growth models neglecting social, political and cultural dimensions of economic activities. A distinction between growth and development, hence, does not make any sense from the conventional point of view when considering the effects of finance on different aspects of social life. The only concern is the growth of investment activities and the proliferation of capital as reflected through the idea of 'capital fundamentalism' (King and Levine 1994), so that finance would become more widespread all over the world, which consecutively leads to spurn developmentalist aims of economic activities.

Beyond growth orientedness, development transcends economic considerations and stimulates a substantial change in the existing functioning of economic, social, legal and political institutions. Thus, development can be defined as a continuous process which paves the way for an equilibrium amongst improvements in different structures (social, economic, political, cultural and *etc*.) through the embedment of morality at the core of whole development agenda, so that any potential of a contradictory situation between these structures is nipped in the bud by the moral mechanism. This approach necessitates that financial structure of an economy should be substantiated with developmentalist perspective, which also reflects the aspirations of Islamic developmentalism, as *rububiyah* and *tazkiyah* concepts essentialise development as a core objective within emancipation and empowerment dimensions of Islam. Thus, finance-development nexus, which is essential to be explored from this point of view, has not been undertaken neither in conventional nor in heterodox economic systems in a systematic manner yet. What have already been studied in the entire literature is finance-growth nexus as response to the basic question about the role of finance on the development of human, society and economy; therefore, hardly any study has attempted to 'go beyond the box' in delving into 'finance-development nexus', which, hence, created a significant gap in the mentioned literature.

This study uncovered that Islamic finance industry has experienced a similar transformation in its objectives through the influences of conventional theoretical underpinnings and practices of financing, although the emergence and existence of Islamic finance initially relates to 'developmentalist' objectives and 'substantive morality' of Islamic moral economy as advanced, in a modern meaning, since 1960s. This argument is evidenced empirically (in the Chapter 2) by examining the relationship between Islamic banking and economic development. Accordingly, the results show that Islamic banking fails to demonstrate positive impact on economic development, thereby implying a poor performance in terms of contributing to developmentalist trajectories of the sampled countries, albeit in the imagination of founding fathers, Islamic economics has envisaged and institutionalised Islamic banking to serve for both financial and social development in a harmony as *tazkiyah* axiom suggests. As Islamic finance could not fulfil such an objective due to the gradual convergence towards mainstream finance, it is concluded that as long as Islamic finance mimics the conventional financialisation trend, empirical studies that examine Islamic banking-development nexus would not have any word other than stating the failure and evidencing this through different estimation models.

This study, therefore, fills this gap by incorporating Islamic developmentalism into the debate within expanding and growing Islamic finance. By the same token, it suggests a re-examination of the role of Islamic finance on economic, social, legal and political structures through breaking 'finance-growth link' and offering a 'finance-development relationship' by considering 'financing' as part of embeddedness. In doing so, this study argues that financial sphere can evade the dominance of capital fundamentalism by considering its position as an instrument to contribute to social good rather than as an end itself. However, what neoclassical economics dictates is the superiority of capital against other factors of production such as labour, land and natural environment. Conventional finance, in this sense, is designed to serve for the proliferation of capital by creating tension with other stakeholders; thereby, financial process can be maintained for the accumulation of capital and profit maximisation of those who maintain capital-intensive investment activities through fictitious commodities. The superiority, in consequence, culminates in the absolute predominance of capital such that individual and social life, factors of production and economic relations all are subordinated to the hegemony of capital with the negligence of developmental outcomes as an objective to accomplish in the policy level.

Islamic economics movement, in contrast to this, aims to decentre the hegemony of capital by rescuing human well-being, land, labour, capital, extended stakeholders and the resulting social formation through giving equal shares and responsibilities for each constituent so that a harmonious growth amongst different stakeholders occurs and develops towards their perfection as suggested by *tawhid*, *rububiyah*, tazkiyah, *adalah* and *ihsan* axiom. This understanding is also reflected in the financial sphere, as the principle of the prohibition of interest is nothing but the rule against the domination of capital in terms of unfair return of capital leading to preserve each stakeholder's right in the production process and financial area. However, as opposed to such an imagination, in the current practice, Islamic finance is criticised on the ground that it invariably favours capital domination within Islamic banks as evidenced in its operational areas including modes of finance, sectorial distribution of financing, and governance structure. For this reason, Islamic banks has never brought about momentous changes in development trajectories of countries wherein they keep operating.

Islamic banks, for instance, intensify their financing modes on fictitious products that resemble conventional financial transactions such as the case with organised *tawarruq*, which is considered to be both un-lawful and immoral as the *fatwa* of International *Fiqh* Academy of OIC states; however, organised *tawarruq* practised by Islamic banks under market pressure and capital efficiency. In a similar manner, in the corporate level, Islamic banks' shareholder value-oriented governance structure is at odds with the ideal Islamic corporate governance, as the statistical records measured for shareholder value orientation evidence. These examples blatantly demonstrate that market system and price mechanism push its own self-regulated nature on Islamic finance and shape its current and future practices to remain with the capital-oriented activities of finance capitalism whereby it gains global recognition. More broadly, Islamic finance is kept within the boundaries of old norms shaped by capital predominance, and hence it is not allowed to constitute an alternative to the prevailing financial system by submitting to the established capital forms and norms rather than re-defining capital as Islamic economics suggests.

This research expands the scope of non-developmental expansion of Islamic finance and its capital fundamentalism through the introduction of the notion of Islamic financialisation, which has barely been associated in the literature of Islamic economics due to an unwitting negligence of the term by practitioners and theoreticians. It is, therefore, argued that the social failure roots in, to a large extent, the adopted *financial logic* borrowed from mainstream economics whereby the utmost importance is given to financial sector to take place and substantialise at the core of economic activities.

In the meantime, the scope of failure is controversially multifaceted; however, this study identifies it with the Polanyian notion of embeddedness. The emergence of Islamic financialisation should, accordingly, be understood as an attempt of disembedding shared norms, values and beliefs from economic realm that eventually leads up to create a self-regulated and standalone sector of Islamic finance, which in return, paves the way for commodifying social relations that no longer embraces its traditional role of sharing and participatory economy, but rather replaces with transactions under the whole objective of efficiency. As in the case of financialisation in advanced economies where financial markets dominate entire economic system with the pursuit of generating profit at the expense of engendering social inequality and distributional problems, Islamic financialisation, far from conceiving developmentalist outcomes, helps creating a sort of financialised commercial society within Muslim domain. The disenchantment with Islamic finance is, hence, pertain to such a process of disembeddedness.

Ideally speaking, Islamic finance should have emerged as a bottom-up demand from society, as parallel to the model developed by Portes (2010), to meet financial needs of individuals under a simple but functional role of 'financing' *vis-à-vis* a self-proclaimed 'finance' understanding constructed by mainstream economics. Nevertheless, it could not position itself within a moral economy or to emerge as a system understanding and has always targeted to shine out as an alternative market segment within global financial system. The gradual process of diverging from moral economy perspective is elucidated through historical facts and conditions of Muslim world surrounded by a new regulation of world financial system in the post-war period. In this sense, Islamic banks borrowed the existing regulations and standards of mainstream financial system to apply over their banking system such as (LIBOR, Basel III, *etc*.); thereby, it was implicitly accepted that the challenges in legal issues, risk natures and operational model can be resolved through conventional prescriptions.

This research associates the elaborated challenges and failures of Islamic finance with methodological obscurity in defining the objectives of Islamic economics. In other words, both developmentalist failure of Islamic finance and the financialisation process ascertained that the initial concern with theory making should be on methodological issues, for knowledge can only be authenticated through a rigorous methodology. In search for addressing methodological dimension, despite being mentioned often in everyday practice, *maqasid al-Shari'ah* has almost been neglected in Islamic economics literature, although it has great potential to function as an essential methodology. Instead, it was made subservient to a justification mechanism maintained with Islamic finance sector. Controversial and disputable issues within the sector have been resolved through a symbolic use of *maqasid al-Shari'ah* and *maslahah* (public interest); thereby, Islamic finance would display a smooth parallel with mainstream financial progress. It is not surprising, in this regard, that *maqasid* perceptions of governments, *Shari'ah* scholars and some academics favouring self-regulated market economy system are all homogenous through the prevalence of form-based understanding with the neglect of substance. Therefore, an economic system which is conceived to reflect Islamic notions but in fact not much different than capitalist framework can only reveal a form-based understanding bounded with methodological individualism, and hence fails to go beyond concerning utility maximisation, essentialisation of price mechanism, market exchange and efficient use of resources. However, proactive *maqasid* understanding removes such a dilemma by channelling both form and substance in the service of social good in a harmonious way.

Beyond instrumental and eclectic approaches, theoretical grounds of Islamic economics should be re-examined in light of the proactive *maqasid al-Shari'ah* framework. By doing so, the rationale behind the failure of realising Islamic developmentalism in post-colonial Muslim nations can better be explained, since proactive *maqasid* envisages an authentic methodology and approach towards developmentalist considerations when compared to existing applications of *maqasid* based on methodological individualism.

It should be re-iterated that morality plays a central role on the entire process of knowledge authentication through *maqasid al-Shari'ah*, while the current use of *maqasid* in Islamic banking and finance demonstrates that it has been relegated to *fiqhi* injunctions and used as an instrument to legalize particular product and operation in a legalistically rational manner. This runs against the expectation that *maqasid al-Shari'ah* should constitute the essential base of methodology for Islamic moral economy, as deductive reasoning based on Islamic ontology and also historical practice suggests that we should constitute Islamic moral economy beyond the narrowly defined Islamic economics as latter refers to *fiqh*, while the former is constituted through essential and pro-active *maqasid*. Thus, substantive morality should be embedded through *maqasid* in the theoretical underpinnings of Islamic economics to generate Islamic moral economy to fit into pro-active *maqasid* expectations as a distinct system of economics, so that *maqasid* objective of 'whatever is done should be in the interest of human well-being and social welfare' can be achieved; otherwise shareholding understanding will not produce the structured social good or *ihsan* as *maqasid* requires stakeholding based operational form and such a political economy. This requires interpersonal and social relations not to be merely relegated to economic relations, but economics and finance should be embedded into norms and values of society through locating ethico-economic relationship across each system so that morality can be articulated beyond impersonal market environment. Thus, *maqasid* or essentialisation of human well-being and social welfare in economic and financial activities takes place by motivating economic forces for economic and human development, which constitutes a base for the articulations of economic and financial choices to be linked to their 'consequences' beyond mere 'intentionalism'.

5.3. LIMITATIONS AND FUTURE RESEARCH

Despite this research aims to develop a new political economy discourse on the idea of Islamic economics and the historical rise of Islamic finance with a trilateral study concentrating on the notions of development, financialisation and *maqasid* methodology, it has some limitations that need to be addressed.

The first limitation is related to the empirical parts conducted in the first two studies. While Islamic development and financialisation are critically approached in a discursive manner, empirical examination of these two topics requires measurable forms of knowledge. Therefore, a thoroughly developed discursive analysis has to meet the challenge of its expression in quantifiable form with equal thoroughness. Acknowledging the limited data pool in different sources and its availability only for developed countries, it becomes a striving task to locate the best indicators for our selected variables and country data. In our case, for instance, Islamic concept of development was expressed in human development index as an indicator of Islamic developmentalism, although it has many limitations as elaborated in the relevant section in Chapter 2.

In addition to the measurement problem, data availability constitutes another aspect of the limitations of empirical analysis. Although mentioned many times in different studies, the unavailability of required data is of special importance for the empirical studies on Islamic banking and finance. Together with the country specific problems on data access (*e.g.* due to their non-professionalism on disclosure issues), there is no proper database yet, to the best of our knowledge, specialised on Islamic banking industry except some naïve attempts or popular databases with simple indicators of Islamic banks. Thus, data collection process takes much time, if there is, as each country specific data has to be picked out separately from their websites.

Another limitation of this research stems from the lack of research in the newly introduced notions of Islamic financialisation, proactive *maqasid* methodology and Polanyian or moral economy perspective towards Islamic finance. Although it shows the authenticity and originality of this research, the limitation is about the limited level of references used in this research and hence made potential comparison with alternative thoughts difficult while it may have contributed to the originality.

Despite our reservations on the shortcomings of statistical methods used in performance measurements, future research may consider constructing an authentic index for Islamic development for evaluating performances of Islamic banks; thereby, the results would better reflect to what extent Islamic banking sector make contributions to development trajectories of countries. In addition, future research can be developed on the dimensions of *maqasid al-Shari'ah* as the methodology of Islamic economics and policy-level outcomes would accordingly be suggested for Islamic banks in the light of *maqasid* understanding. Lastly, the conceptualisation of Islamic financialisation can be further developed through expanding its dimensions on different spheres of everyday life. Potential indicators can be constructed amongst Islamic finance industry outlook for this end.

5.4. EPILOGUE

This research aimed at gaining a new insight on the emergence and development of Islamic economics and finance based on the challenges in realising its aspirations within Islamic political economy understanding. In doing so, it empirically examined development and financial performance of Islamic banks to shed light on their potential contributions to the development trajectories of the sampled countries. With the recognition of social failure, this research approached the development and social failure of Islamic finance project from the perspective of financialisation, since the failure, to a large extent, can be explained in the adopted financial logic borrowed from mainstream economics and market economy. Lastly, it is argued that developmentalist failure and the resulting financialisation mainly stem from the lack of a methodological dimension that must be applied over theorisation of Islamic economics. In this manner, this research constructed an extended proactive *maqasid* framework to be incorporated into the theory making of Islamic economics. In conclusion, as the discursive and empirical analyses in each of the preceding chapter demonstrate, this research has fulfilled both its main aim identified in Chapter 1 and the aims of each essays.

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APPENDIX TABLE

Table A.2.1: Banking Sector Development and Economic Growth

Study	Sample	Method	Key Findings
Goldsmith (1969)	Cross section of 35 countries (19 developed and 16 less developed) from 1860-1963	OLS and graphical analysis	A clear relationship between financial intermediation and economic growth, but the correlation coefficient is weak for developed countries
King and Levine (1993)	Pooled cross section of 80 countries over the 1960-1989 period	Ordinary Least Squares (OLS)	Total factor productivity, capital accumulation and real per capita GDP have strong association with the defined indicators of financial development, which then supports the Schumpeter's ideas that finance is a key for growth
Demetriades and Liuntel (1996)	Annual observations for India from 1961 to 1991	Error-correction model (ECM), exogeneity tests and principal component analysis (PCA)	Based on the findings it is evidenced that financial development and growth are jointly determined. Controlling banking sector undermines the process of financial development through inhibiting financial deepening
Odedokun (1996)	Times series of 71 developing countries over varying periods between the1960s and 1980s	OLS	Financial intermediation has substantial role over growth and it promotes economic growth in roughly 85% of the countries
Rousseau and Wachtel (1998)	Historical evidence from 5 industrialised countries (the USA, the UK, Canada,	Vector error correction and vector auto regression model	Generally, financial factors accelerate industrialisation process of these countries significantly. The activities of real sector are, on the other hand, supported much by financial intermediation.

	Norway and Sweden) from 1870-1929		
Demirgüç-Kunt and Maksimovic (1998)	Annual data of 30 developing and developed countries for the period 1980–1991	OLS	The study shows that large banking sector within the existence of efficient legal systems and active stock markets easily provides external funds for firms, which, in turn, facilitates firm's growth.
Rajan and Zingales (1998)	41 countries with industry-level data for the period 1980–1990	OLS and panel data fixed effects	The results show that industries with a high reliance on external finance develop more within their improved financial intermediation institutions. External finance, here, enables rapid growing firms through easing capital flow.
Levine (1998)	Annual data for 42 countries covering the period 1976–1993	OLS and generalised method of moments (GMM)	Similar to the study of Demirguc-Kunt and Maksimovic (1998), this study finds that if banking sector is supported by strong legal systems, it contributes to GDP growth in a faster pattern.
Harrison, Sussman, and Zeira (1999)	US state level data from 1965-1995	Granger causality and two stage regressions models	There is a significant negative relationship between the cost of financial intermediation and economic development;
Ram (1999)	Annual data for 95 countries over the period 1960–1989	OLS	The results show that the correlation between financial development and economic growth in these countries are found to be negligible. Even regression analysis on each individual country gives similar results.
Xu (2000)	Annual data for 41 countries over the period 1960–1993	VARs and impulse response analyses (IRA)	The results evidences that finance plays a key role for growth through channelling investment. In specific, 27 countries out of 41 have positive effects of financial development on investment growth and economic growth.

Cetorelli and Gambera (2001)	41 countries of which 36 industries are all selected from the manufacturing sector between 1980 and 1990.	OLS	The empirical evidence indicates that bank concentration has a first-order negative effect on growth. However, it is also found that sectors that are more dependent on external finance enjoy a beneficial effect from a concentrated banking sector.
Beck and Levine (2002)	Annual data from 1980 to 1990 on a panel of 42 countries and 36 manufacturing industries	OLS and Two Stage Least Squares (TSLS)	Consistent with the findings of the work of Rajan and Zingales (1998), this study results that more advanced countries within sound legal systems perform fast economic grow through enjoying external finance. However, bank based or market based financial system does not seem to matter for growth.
Thangavelu and Ang (2004)	Quarterly data for Australia from 1960Q1 to 1999Q4	VARs and Granger causality	Financial development indicators pertaining to financial intermediaries suggest that banking sector reacts to the demand created by economic development. Hence, a reverse causality runs from growth to finance. Furthermore, the study is in consistence with the Schumpetarian line that stock markets are vital in promoting economic growth.
McCaig and Stengos (2005)	Annual data for 71 countries from 1960 to 1995	GMM	The study indicates that if private domestic credit or liquid liabilities is used as the measure of financial development, positive effect of finance on growth is seen strong. However, if the ratio of commercial bank assets to central bank assets is used as the indicator of financial development, the effect becomes weak.

Ang (2009)	Annual data for Malaysia from 1965 to 2004	VECM, Johansen cointegration, Granger causality and PCA	The study examines the FDI-growth nexus in Malaysia by controlling for the level of financial development. Financial development is measured by a composite index, which is a summary measure of four financial development indicators. The results show that FDI and financial development are positively related to output in the long run. The impact of FDI on output is enhanced through financial development.
Poshakwale and Qian (2011)	Bank-specific data in Egypt during 1992 2007	The conjectural variation (CV), The seemingly unrelated regression (SUR)	The results show that financial reforms lead to competitiveness and production efficiency of banking sector, which, in turn, yields robust economic growth. The study suggests a significant relationship between financial bank productive efficiency and economic growth in the short run but not in the long run.
Morck, Yavuz, and Yeung (2011)	2001 global sample of 244 banks that Caprio, Laeven, and Levine (2007) used in their studies	OLS	The study concludes that less efficient capital allocation is observed in countries whose banking systems are more thoroughly controlled by tycoons or families. The magnitude of this effect is similar to that of state control over banking industry. Unlike state control, tycoon or family control also correlates with slower economic and productivity growth, greater financial instability, and worse income inequality.
Samila and Sorenson (2011)	An unbalanced panel covering all 329 Metropolitan Statistical Areas (MSAs) in the United States from 1993 to 2002.	Fixed-effects IV estimates	It is found that increases in the supply of venture capital positively affect firm starts, employment, and aggregate income. The findings are quite consistent with the notion that an expansion in financial intermediation improves the allocation of capital and therefore can stimulate growth.

Chen, Lee, and Lee (2012)	Panel data for a maximum of 60 countries covering the period 1976–2005	OLS	The article investigates the effect of life insurance on economic growth and what conditions affect the insurance-growth nexus. The main findings confirm the positive impact of the development of the life insurance market on economic growth.
Beck, Georgiadis, and Straub (2014)	Panel data of 132 countries for the period between 1980 and 2005.	GMM	We find that an expansion of credit has a positive effect on per capita output growth only up to a point. Beyond this threshold the impact of finance on growth is not statistically significant anymore.
Cheng, Ho, and Hou (2014)	Annual data from 15 industrial and 15 emerging countries over the period from 1976 to 2005	Pooled mean group estimation	The results suggest that banking development and stock market development may have distinct short-and long-run impacts on economic growth at various stages of country development. Financial development is not always a panacea for economic growth. Most importantly, the findings suggest that the fully functional tools to render stable growth for a country may depend on the level of the country's development.
Samargandi, Fidrmuc, and Ghosh (2015)	A panel of 52 middle income countries over the 1980–2008 period	Pooled mean group estimations	There is an inverted U-shaped relationship between finance and growth in the long run. In the short run, the relationship is insignificant. This suggests that too much finance can exert a negative influence on growth in middle-income countries.

Table A.2.2: Causality between Finance and Economic Growth

Study	Sample	Method	Key Findings
Gupta (1984)	Quarterly time series data from 1961Q1 to 1980Q4 for 14 developing countries	Vector autoregression models (VARs) and Granger causality	The results showed that finance leads growth with causality running from financial systems to economic sector. Although a case may be argued for a reverse causality, there is weak evidence for two-way causality.
Jung (1986)	Times series of 56 countries from 1950-1980	VARs and Granger causality	Less developed countries perform a causal relationship which runs from financial development to economic growth, but developed countries are observed to have a reverse causal pattern.
Demetriades and Hussein (1996)	Annual data for 16 countries with at least 27 continuous annual observations	VARs, vector error-correction model (VECM), Engle–Granger cointegration, Johansen cointegration and Granger causality	The causality test results depict weak evidence about finance leading to growth, but rather the relationship has a bidirectional pattern where growth and finance are jointly determined.
Neusser and Kugler (1998)	Annual data for 13 OECD countries for the period 1970–1991	Johansen, Stock Watson, Horvath Watson, Phillips Ouliaris, Engle–Granger cointegration and Granger causality	Through using financial sector GDP and manufacturing GDP as proxies for financial development and economic growth, respectively, the causality test endorses that finance substantially matters for economic growth by manufacturing TFP.

Luintel and Khan (1999)	10 developing countries from 1951-1995	Multivariate vector auto regression model	There is a bi-directional causality between financial and real sector for all countries.
Calderon and Liu (2003)	Pooled data of 109 developing and industrial countries from 1960 to 1994	Panel VAR, Geweke decomposition and Granger causality	The empirical evidence indicates a bidirectional causality between financial development and economic growth. Finance functions more properly in developing countries. Bu generally, it fosters growth through channels of capital accumulation and productivity growth.
Christopoulos and Tsionas (2004)	Annual data for 10 developing countries, from 1970 to 2000	Panel VECM, panel cointegration, threshold cointegration and fully modified OLS	The evidence indicates a long-run equilibrium relationship between financial development and economic growth. The long-run causality runs from finance to growth, but there seems no sign for short run causality.
Ketteni, Mamuneas, Stengos, and Savvides (2007)	Panel data of 74 countries for the period 1961–1995	Semiparametric partial linear model	This study finds that finance–growth nexus appears to be nonlinear when the nonlinearities between economic growth and initial per capita income are not taken into account. However, when these nonlinearities are neglected the relationship can only appear to be linear.
Handa and Khan (2008)	Time series data on a cross-section of 13 countries from 1960 to 2002	Cointegration analysis and Granger causality	The results show that for Bangladesh, Sri Lanka, Brazil, Malaysia, Thailand and Turkey, causality runs from economic growth to financial development. Granger-causality is bi-directional for India, Argentina, Germany, Japan, the UK and the USA. There does not exist one-way Granger-causality from financial development to economic development for any of the countries examined.
Hassan, Sanchez, and Yu (2011)	168 countries from 1980–2007	Panel regressions, Short-term multivariate analysis	There is a two-way causal relationship between finance and growth for most regions and one-way causality from growth to finance for the two poorest regions.

Kar, Nazlioglu, and Agir (2011)	Panel data of 15 MENA countries for the period 1980–2007	Bootstrap panel Granger causality analysis	Empirical results show that the direction of causality between financial development and economic growth is sensitive to the measurement of financial development in the MENA countries. Therefore, the direction of causality seems to be country and financial development indicator specific.
Hsueh Hu, and Tu (2013)	Panel data of 10 Asian countries surveyed during period 1980 to 2007	Bootstrap panel Granger causality analysis	The results show that the direction of causality between financial development and economic growth is sensitive to the financial development variables used in the ten Asian countries examined in this work. Moreover, the findings support the supply-leading hypothesis, as many financial development variables lead economic growth in some of the ten Asian countries surveyed, especially in China.
Pradhan, Arvin, Hall, and Bahmani (2014)	Panel data of ASEAN countries for the period 1961–2012	PCA and panel vector auto-regressive model	The study finds the presence of both unidirectional and bidirectional causality links between these variables.
Peia and Roszbach (2015)	Time series analysis of 22 advanced economies for the period between 1973 and 2011	Panel cointegration and causality	The results suggest that causality patterns depend on whether countries' financial development stems from the stock market or the banking sector. These findings indicate that the direction of causality between finance and growth is likely to be different at high levels of development.
Gould, Melecky, and Panterov (2016)	Cross section of 100 countries over 1970–2014	Causality analysis	The results confirm that the previous findings of the literature that financial deepening, and credit to GDP in particular, could be an ambiguous measure of financial development because, although its linear effect is positive, its quadratic effect is significantly negative.

Table A.2.3: Financial Deepening, Repression and Financial Liberalisation

Study	Sample	Method	Key Findings
Roubini and Sala-i-Martin (1992)	Cross-section of 98 countries for the period 1960-1985	Cross country regressions	Various measures of financial repression have negative effects on growth
De Gregorio and Guidotti (1995)	Annual data of 99 countries for the period 1960-1985; and Panel data of 12 Latin American countries during 1950–1985	OLS and panel data random effects	Financial development accelerates economic performance of countries, but the example of Latin American countries shows that financial liberalisation without proper regulation policies negatively effects the role of finance over growth.
Demetriades and Luintel (1997)	Annual data for India from 1960 to 1991	Engle–Granger cointegration, Stock–Watson cointegration, PCA and weak exogeneity tests	Financial repression through repressionist controls is found to have substantial negative effects on financial development. Financial development and economic growth are jointly determined.
Demetriades and Luintel (2001)	Annual data for South Korea from 1956 to 1994	ECM and PCA	Financial restraint policies functions significantly in the financial development process of South Korea. Nonetheless, real interest rate effects on financial development are insignificant.
Deidda and Fattouh (2002)	Cross-country data for 119 countries over the period 1960-1989	Threshold OLS model	The link between financial depth and economic growth is positive only in high income subsample. For low income countries, there is no such significance. This study concludes that there is nonlinear relationship between finance and growth.

Arestis, Demetriades, Fattouh, and Mouratidis (2002)	Annual data for six developing countries for the period 1955–1997	VECM, Johansen cointegration and PCA	The net effect of financial liberalisation considerably varies across countries. Real interest rate, on the other hand, has a positive impact on four out of the six countries.
Braun and Raddatz (2008)	Industry-level data for a large cross-section of 41 countries that liberalised trade during 1970 to 2000	PCM	The results show that the strengthening of promoter relative to opponent industries resulting from liberalisation is a good predictor of subsequent financial development. The benefits of developing the financial system are insufficient for financial development, and rents in particular hands appear to be necessary to achieve it.
Amaral and Quintin (2010)	A sample of 137 countries with the data for at least 20 years leading up to 1994	OLS	It is observed that poor enforcement in an economy direct less capital to the production sector and employ less efficient technologies. Also, the average scale of production should rise with the quality of enforcement.
Rousseau and Wachtel (2011)	Cross-sectional and panel data on financial and macroeconomic indicators for 84 countries over the period from 1960 to 2004	Time period fixed effects and GMM dynamic panel estimation	Excessive financial deepening or too rapid a growth of credit may have led to both inflation and weakened banking systems which in turn gave rise to growth-inhibiting financial crises. Excessive financial deepening may also be a result of widespread financial liberalisations in the late 1980s and early 1990s in countries that lacked the legal or regulatory infrastructure to exploit financial development successfully. However, there is little indication that liberalisations played an important direct role in reducing the effect of finance.

Table A.2.4: Stock Market Development and Growth

Study	Sample	Method	Key Findings
Atje and Jovanovic (1993)	Annual observations for 94 countries during the period 1960–1985	OLS	Stock markets have large effects in stimulating economic growth. However, the study failed to find similar effects of bank lending.
Harris (1997)	Annual data for 39 countries over the period 1980–1988	Two stages least squares (2SLS)	The results find no evidence about the promoting role of stock market activities over growth per capita output. While stock markets have an insignificant role in less developed countries, it has some functions in developed countries.
Levine and Zervos (1998)	Cross-section of 47 countries from 1976 to 1993	OLS	The study concludes that initial level of stock market liquidity is a good predictor for growth, but that of market capitalisation, stock return volatility, stock market integration is not robustly linked with growth.
Rousseau and Wachtel (1998)	Cross-section of 47 countries from 1980 1995	(2SLS) and panel VAR	The study evidences for causality running from both stock market indicators (per capita value traded and market capitalisation, scaled by a price index) to economic activity. Furthermore, the adjustment of the stock market indicators with a general price index overstates the effect of market capitalisation on economic activity. Finally, the study concludes that liquidity of stock markets is more important than size.

Henry (2000)	Annual data for 11 developing countries spanning the 1970s and 1990s	A range of panel data techniques	The study shows that stock market liberalisation accompanies with increased private investment in 9 out of 11 countries studied.
Arestis, Demetriades, and Luintel (2001)	Quarterly data for five developed countries, including Germany, the USA, Japan, UK and France over the period 1968–1998	Johansen cointegration, VECM and weak exogeneity tests	While banks and stock markets both foster economic growth, the significance of the latter is relatively weak compared to that of banks. Furthermore, the results suggest that stock market volatility has negative real effects in Japan, France and the UK.
Caporale, Howells, and Soliman (2005)	Quarterly data from 1979Q1 to 1998Q4 for Chile, Malaysia, Korea and the Philippines	VARs and modified WALD (Toda Yamamoto) tests	The study explores the stock market development and growth link. It concludes that causality runs from stock market development to growth through increasing investment efficiency.

Table A.2.5: Political, Social and Legal Factors, Regulation, Governance

Study	Sample	Method	Key Findings
Levine (1999)	Annual data for 49 countries over the period 1960–1989	GMM	The results show that financial development and economic growth are highly associated. Financial systems of those countries which perform sound and efficient legal and regulatory framework are much developed.
Kroszner and Strahan (1999)	Various state level data from 1975 to 1991	OLS panel regression	This paper investigates private-interest, public-interest, and political institutional theories of regulatory change to analyse state level deregulation of bank branching restrictions. Using a hazard model, it is found that interest group factors related to the relative strength of potential winners (large banks and small, bank-dependent firms) and losers (small banks and the rival insurance firms) can explain the timing of branching deregulation across states during the last quarter century. Deregulation occurs earlier in states with fewer small banks, in states where small banks are financially weaker, and in states with smaller, presumably bank-dependent, firms.
Pagano and Volpin (2005)	Panel data of 47 out of the original 49 countries studied by LLSV (1998)	Panel estimation techniques and questionnaire	The study analyses the political determinants of investor and employment protection which are good indicators for sound financial systems, which, in turn, fosters economic growth. The model predicts that proportional electoral systems are conducive to weaker investor protection and stronger employment protection than majoritarian systems. The proportionality of the voting system is significantly and negatively correlated with shareholder protection in a panel of 45 countries, and positively correlated with employment protection in a panel of 21 OECD countries. Other political variables also affect regulatory outcomes, especially for the labor market.

Papaioannou and Siourounis (2008)	A maximum of 166 countries between 1960–2003	Fixed effect estimator	The study aims to examine 'within country growth effect of democratisation'. Results evidence that democratisation leads to almost a 1% increase in real annual per capita GDP growth.
Cheng and Degryse (2010)	The dataset contains annual growth rates of real per capita GDP, real per capita capital stock, and FDI for 27 Chinese provinces over the period 1995–2003	OLS	The study examines whether the financial development of two different types of financial institutions — banks and non-banks — have a (significantly different) impact on local economic growth. The findings indicate that banking development shows a statistically significant and economically more pronounced impact on local economic growth.
Jeanneney and Kpodar (2011)	a large sample of developing countries with panel data over the period 1966–2000	OLS and GMM	In regions where financial instability goes along with financial development, financial instability is detrimental to growth and poverty alleviation, which lowers the beneficial impact of financial development.
Benmelech and Moskowitz (2010)	33 states with a 40 years data of 19th century America	OLS	The study examines the political economy of one of the oldest forms of financial regulation, usury laws, and links it to financial development in the United States in the 19th century. In line with this, it aims to explore whether usury laws (as a measure of financial development) have any impact on economic development. The evidence suggests that incumbents with political power apply stringent usury laws because they impede competition from potential new entrants who are credit rationed.
Körner and Schnabel (2011)	77 countries over the period 1970–2007	OLS	The study explores the impact of public ownership in the banking system on subsequent per capita GDP growth. It is found that in hardly developed

			countries with low financial development and poor political institutions, the impact of public ownership of banks on economic growth is strongly negative.
Park (2012)	76 macroeconomic data from various countries over the period 2002–2004.	Cross sectional regressions	The paper explores the impact of corruption on both the banking sector and economic growth. The results evidence that corruption significantly aggravates the problems with bad loans in the banking sector. Corruption also distorts the allocation of bank funds from normal projects to bad projects, which decreases the quality of private investments, hence it decreases economic growth.
Mclean, Zhang, and Zhao (2012)	A sample of firms drawn from 44 countries during the period 1990 to 2007	Country-level regression	Strong investor protection leads countries to enjoy and benefit from external financing more effectively. More generally, this study suggests that investor protection promoting accurate share prices, reducing financial constraints, and encouraging efficient investment.
Anwar and Cooray (2012)	Panel data in South Asia over the period 1970 to 2009	OLS and GMM	The paper focuses on the impact of the interaction of (i) financial development and foreign direct investment and (ii) financial development and the quality of governance on economic growth in South Asia. It founds that financial development has contributed to an increase in the benefits of FDI in South Asia. In addition, improvement in political rights and civil liberties (which are used as a proxy for the quality of governance) has also enhanced the benefits of financial development in South Asia.
Aisen and Veiga (2013)	A sample covering up to 169 countries, and 5-year periods from 1960 to 2004	GMM	The study explores the effects of political instability on economic growth. Results show that higher degrees of political instability are associated with lower growth rates of GDP per capita. Political instability adversely affects growth by lowering the rates of productivity growth and, to a smaller degree, physical and human capital accumulation. Finally, economic freedom and

			ethnic homogeneity are beneficial to growth, while democracy may have a small negative effect.
Brown, Martinsson, and Petersen (2013)	A broad sample of firms (approximately 5,300 firms) across 32 countries over the period 1990 to 2007	OLS	Strong shareholder protections and easing stock market financing lead to achieve long-run rates of R&D investment. These findings connect law and stock markets with innovative activities key to economic growth.

Table A.2.6: Political Regimes and Growth[53]

Author	Sample	Time Period	Key Findings
Przeworski (1966)	57 countries	1949-1963	dictatorships at medium development level grew fastest
Adelman and Morris (1967)	74 underdeveloped countries (including communist block)	1950-1964	authoritarianism helped less and medium developed countries
Dick (1974)	59 underdeveloped countries	1959-1968	democracies develop slightly faster
Huntington and Dominguez (1975)	35 poor nations	the 1950s	authoritarian grew faster
Marsh (1979)	98 countries	1955-1970	authoritarian grew faster
Weede (1983)	124 countries	1960-1974	authoritarian grew faster
Kormendi and Meguire (1985)	47 countries	1950-1977	democracies grew faster
Kohli (1985)	10 underdeveloped countries	1960-1982	no difference in 1960s; authoritarian slightly better in 1970s
Landau (1986)	65 countries	1960-1980	authoritarian grew faster

[53] Table A.2.6 is directly taken from Przeworski and Limongi (1993:61).

Sloan and Tedin (1987)	20 Latin American countries	1960-1979	bureaucratic-authoritarian regimes do better than democracy; traditional dictatorships do worse
Marsh (1988)	47 countries	1965-1984	no difference between regimes
Pourgerami (1988)	92 countries	1965-1984	democracies grew faster
Scully (1988, 1992)	115 countries	1960-1980	democracies grew faster
Barro (1991)	72 countries	1960-1985	democracies grew faster
Grier and Tullock (1989)	59 countries	1961-1980	democracy better in Africa and Latin America; no regime difference in Asia
Remmer (1990)	11 Latin American countries	1982-1988	democracy faster, but result statistically insignificant
Pourgerami (1991)	106 less developed countries	1986	democracies grow faster
Helliwell (1994)	90 countries	1960-1985	democracy has a negative, but statistically insignificant, effect on growth

Table A.2.7: Financial Development and Human Development

Author	Sample	Method	Key Findings
Outreville (1999)	A cross-sectional analysis of 57 developing countries	OLS	The empirical results indicate that human capital and socio-political stability are important factors in explaining the level of financial development of these markets.
Monacelli, Iovino and Pascucci (2012)	Panel data of 68 countries over 1990-2005 period	OLS, Difference-GMM and 2SLS	The results suggest that (1) improvements of financial market depth, measured by stock market capitalisation to GDP, are robustly correlated with changes of HDI; (2) financial policy enhancements are associated to a positive HDI variation; (3) the main channels through which financial reforms acts are policies connected with: credit controls and excessive reserve requirements, interest rate controls, bank privatisation, banking supervision and regulation.
Ostojic (2013)	Panel data of European Union countries between 1990-2010	OLS	The results show that financial development has a strong positive relationship with human development and that several characteristics of the financial system are highly correlated with human development.
Sehrawat and Giri (2014)	Time series data of India from 1980-2012	Cointegration analysis	The results of Granger non-causality indicate that unidirectional causality runs from financial development indicators to human development index (HDI). The variance decomposition analysis shows that among all the financial indicators, broad money supply (M3) has the largest contribution to changes in human development in India.

Asongu and Nwachukwu (2015)	A panel of 38 African countries with data for the period 1996-2008	2SLS, Fixed Effects, GMM and Tobit regressions	The main finding is that financial dynamics of depth, activity and size improve inclusive human development, whereas the inability of banks to transform mobilised deposits into credit for financial access negatively affects inclusive human development.
Filippidis and Katrakilidis (2015)	Panel data from 52 developing economies during 1985–2008	Differenced-GMM	The results demonstrate that: (i) institutional quality can explain international differences in the level of banking sector development; (ii) economic institutions and human development are extremely significant for banking sector development; (iii) the legal system is the dominant dimension of economic institutions; and (iv) the combined reforms of economic institutions matter more than separate institutional reforms.
Park and Shin (2017)	Sample period spanning 1960 to 2011, covering 162 countries	OLS and Granger Causality	Main findings suggest that financial development contributes to reducing inequality up to a point, but as financial development proceeds further, it contributes to greater inequality. We also find that when the ratio of primary schooling to total schooling increases and law and order improves, financial development becomes more effective in reducing inequality.

Table A.2.8: Islamic Banking Development and Economic Growth

Study	Sample	Method	Key Findings
Bashir (2003)	Cross country bank level data of 8 Middle Eastern countries between 1993 and 1998	Pooled OLS	The results indicate that high leverage and large loans to asset ratios lead to higher profitability. The results also indicate that foreign owned banks are more profitable than their domestic counterparts. Everything remaining equal, there is evidence that implicit and explicit taxes affect the bank performance measures negatively.
Rosly and Abu Bakar (2003)	IBS banks in Malaysia over the period 1992-1999	OLS	The study found that Islamic banking scheme (IBS) banks have recorded higher return on assets (ROA) as they are able to utilize existing overheads carried by mainstream banks. Although Islamic credit finance products may have complied with *Shari'ah* rules, their lack of ethical content is not expected to motivate IBS banks to strive for efficiency through scale and scope economies.
Yudistira (2004)	18 Islamic banks over the period 1997-2000	Data Envelopment Analysis	The results suggest that Islamic banks suffer slight inefficiencies during the global crisis 1998-9. Efficiency differences across the sample data appear to be mainly determined by country specific factors.

Furqani and Mulyany (2009)	Quarterly time series data (1997:1 – 2005:4) of Malaysia	Cointegration test and Vector Error Model (VECM)	In the short-run only fixed investment that granger cause Islamic bank to develop for 1997:1-2005:4. Whereas in the long-run, there is evidence of a bidirectional relationship between Islamic bank and fixed investment and there is evidence to support demand following hypothesis of GDP and Islamic bank, where increase in GDP causes Islamic banking to develop and not vice versa.
Goaied and Sassi (2010)	Unbalanced panel data from 16 MENA region countries between 1993-2006	GMM	The empirical results show no significant relationship between banking and growth which reinforce the idea that banks don't spur economic growth. Another finding is that Islamic banks don't make the exception in the financial markets and show a weak relation with growth, but it tends to act positively.
Abduh and Chowdhury (2012)	The quarterly time-series data (Q1:2004 to Q2:2011) of Bangladesh	Cointegration analysis and Granger causality	Islamic bank financing is found to have a positive and significant relationship with economic growth both in the long and short run. It implies that the development of Islamic banking is one of the policies, which should be considered by the government to improve their income.
Abduh and Omar (2012)	The quarterly time-series data (2003:1-2010:2) of Malaysia	Cointegration and error correction models	The results demonstrate a significant relationship in short-run and long-run periods between Islamic financial development and economic growth. The relationship, however, is neither Schumpeter's supply-leading nor Robinson's demand-following. It appears to be bi-directional relationship.

Farahani and Dastan (2013)	Quarterly data (2000:1-2010:4) of 9 Muslim countries	Panel cointegration	The results generally signify that, in the long run, Islamic banks' financing is positive and significantly correlated with economic growth and capital accumulation in these countries. The results obtained from the Granger causality test reveal a positive and statistically significant relationship between economic growth and Islamic banks' financing in the short run and in the long run.
Gheeraert and Weill (2015)	A sample of 70 countries over the period 2000-2005	Stochastic frontier approach	The results indicate that Islamic banking development favors macroeconomic efficiency. Also, Increasing Islamic banking development enhances efficiency until a certain point beyond which expansion of Islamic banking becomes detrimental for efficiency.
Yusof and Bahlous (2013)	Annual data of Malaysia, Indonesia and the Gulf countries for the period of 2000-2009	Panel cointegration analysis, variance decompositions (VDCs) and impulse response functions	Islamic banking is found to contribute to economic growth both in the long run and the short run for both GCC countries and the selected East Asia (EA) countries. In the short run however, Islamic banking contributes more to economic growth in Malaysia and Indonesia compared to the GCC countries.
Gheeraert (2014)	A sample of 32 Muslim countries over the period 2000-2005	OLS	It is found that the development of Islamic banking in Muslim countries leads to a higher banking sector development. It is also evidenced that the Islamic banking sector acts as a complement to the conventional banking in Muslim countries, when both systems co-exist, and the Islamic sector reaches a medium penetration in the total banking sector.
Grassa and Gazdar (2014)	Panel data of five GCC countries for the period 1996-2011	GLS, OLS and Fixed Effect Estimator	Empirical results strongly support the hypothesis that Islamic finance leads to growth in the five GCC countries, however, no significant relationship observed between conventional financial development and growth.

Tabash and Dhankar (2014)	Time series data of Qatar, Bahrain and UAE over the period 1990-2008	The unit root, Cointegration and Granger causality	Empirical results signify that in the long run Islamic banks' financing is positive and significantly correlated with economic growth in the select countries which reinforces the idea that a well-functioning banking system promotes economic growth.
Uddin and Masih (2015)	Time series data of Malaysia over the period 1973-2013	Autoregressive Distributed Lag model (ARDL)	The study finds that there is a long-term relationship between finance, growth and human development. Human development is found significantly correlated with the growth in the long run. However, oil price is found not correlated with growth in the long run for the Malaysian economy.
Imam and Kpodar (2016)	A sample of 52 developing economies, using data over the period 1990-2010	System-GMM, Pooled OLS, Fixed Effect estimator	The results show that, notwithstanding its relatively small size compared to the economy and the overall size of the financial system, Islamic banking is positively associated with economic growth even after controlling for various determinants, including the level of financial depth.

Table A.2.9: Generally Used Financial Development and Economic Growth Indicators

Study - Sample	Financial Development (FD) and Economic Growth (EG) Indicators	Methods
(Estrada *et al.* 2010) a cross-country panel data set covering 116 economies (of which 22 are ADB members) with four nonoverlapping 5-year periods from 1987 to 2008.	FD Indicators: 1- Total liquid liabilities relative to GDP 2- Total liquid liabilities relative to GDP 3- Stock market capitalisation relative to GDP 4- capital inflows relative to GDP (financial openness) Control Variables: 1- Initial GDP per capita 2- Years of schooling 3- quality of governance by including the executive constraint indicator from Polity IV (Marshall and Jaggers 2009), which measures the extent of institutionalised constraints on the decision-making powers of chief executives 4- trade openness, inflation, and government consumption EG Indicator: -average of GDP per capita growth	Fixed Effect
(Goaied and Sassi 2010)	Islamic Financial Development Indicator: 1- the amount of credit issued to the private sector by Islamic banks FD Indicators:	GMM estimation of a dynamic panel model

an unbalanced panel data from 16 MENA region countries observed from 1962 to 2006	1- M3/GDP 2- the value of loans made by deposit money banks and other financial institutions to the private sector <u>Control Variables:</u> 1- the ratio of exports plus imports to GDP (as a measure of trade openness of the economy) 2- the inflation rate (INF) 3- the ratio of government consumption to GDP <u>EG Indicator:</u> -GDP per capita growth	
(Wu *et al.* 2010) a panel data set comprised of 13 countries in European Union (EU) over the period of 1976–2005	<u>Banking development:</u> 1- financial depth measured by the ratio of liquid liabilities of the financial system to gross domestic product (GDP), 2- the ratio of deposit money banks' domestic assets to the sum of domestic assets in deposit money banks and the central bank <u>Stock market development:</u> 1- the ratio of market value of domestic shares listed on domestic exchanges to GDP, 2- the value of the trades of domestic shares on domestic exchanges divided by the value of listed domestic shares <u>Economic development:</u>	Panel unit-root tests Panel mean group (PMG) estimators

	-real GDP in which nominal GDP is expressed by the US dollar	
(Hye 2011) Indian Economy from 1978 to 2008	<u>Quoted FD Indicators:</u> 1- liquid liabilities to nominal GDP; 2- commercial bank assets to commercial bank assets plus central bank assets and 3- domestic credit to private sectors divided by nominal GDP 4- the ratio of total bank deposit liabilities to GDP; the ratio of clearing house amount to GDP; 5- the ratio of the private credit to GDP, 6- the ratio of the stock market capitalisation to GDP <u>FD indicators in this study:</u> 1- market capitalisation of listed companies as a percentage of GDP, 2- liquid liabilities (M3) as a percentage of GDP, 3- domestic credit to private sector as a percentage of GDP 4- ratio of broad money (M2) to narrow money (M1)	Augment Dickey Fuller, Phillips Perron and Ng Perron unit root tests auto-regressive distributed lag approach
(Hassan *et al.* 2011) Panel data of 168 countries with the sample period 1980–2007	<u>FD indicators:</u> 1- domestic credit provided by the banking sector as a percentage of GDP (DCBS) 2- domestic credit to the private sector as a percentage of GDP (DCPS) 3- the broadest definition of money (M3) – as a proportion of GDP	<u>Panel regressions</u>: OLS and WLS <u>Multivariate time-series models:</u> vector autoregressive (VAR) models

	4- the ratio of gross domestic savings to GDP (GDS). 5- the ratio of trade to GDP (TRADE) 6- the ratio of general government final consumption expenditure to GDP (GOV)	
(Yilmazkuday 2011) A panel of five-year averages of standard variables for 84 countries from 1965 to 2004.	EG Indicator: -GDP per capita growth rates FD Indicators: 1- log initial per capita GDP 2- log initial secondary enrollment rate (SEC) 3- the ratio of liquid liabilities (i.e., M3) to GDP 4- the ratio of M3 less M1 to GDP 5- inflation rate (average annual growth rate of the consumer price index (CPI)), Control variables: 1- Openness (measured as residuals from a regression of international trade (the sum of exports and imports) as a percentage of GDP on country size (measured by log GDP) and income level (measured by log per capita GDP) 2- government size	rolling-window two-stage least squares regressions
(Bittencourt 2012)	EG Indicator: growth rate of real per capita output FD Indicators: 1- the ratio of the liquid liabilities to GDP (M2) 2- private bank credit over bank deposits	principal component analysis

panel time-series data of four Latin American countries (Argentina, Bolivia, Brazil and Peru) between 1980 and 2007	3- deposit money bank claims over deposit money bank and central bank claims 4- stock market capitalisation over GDP Control variables: 1- government's share in the real GDP (GOV) 2- the ratio of exports and imports to real GDP (OPEN) 3- the ratio of investment to real GDP (INV) 4- average years of schooling of those aged 25 and over with urbanisation rates (from the World Development Indicators files) to construct an index for structural development (DEV) EG Indicator: The growth rates of the real GDP per capita (GROW)	
(Yusof and Bahlous 2013) Malaysia, Indonesia and the Gulf Cooperation Council (GCC) countries for annual data for period of 2000-2009	Economic growth: GDP per capita (GDPPC) growth Islamic banking system development: Total financing of Islamic banks as a percentage of GDP Stock market development: Total value of stocks traded as a percentage of GDP Gross fixed capital formation: Gross fixed capital formation as a percentage of GDP as an economic indicator for investment Control economic variable: Volume of trade as a percentage of GDP as an indicator of the economic variable	panel cointegration analysis, variance decompositions (VDCs) and impulse response functions

(Hsueh *et al.* 2013) A panel data for the causality between FD and EG among ten Asian countries surveyed during period 1980 to 2007	FD indicators: 1- DC/GDP: the ratio of domestic claims to GDP 2- M1/GDP: the ratio of money supply M1 to GDP 3- M2/GDP: the ratio of money supply M2 to GDP 4- M3/GDP: the ratio of money supply M3 to GDP EG Indicator: -real GDP	Bootstrap panel Granger causality analysis
(Kouki 2013) panel data of four countries of the North African region (Algeria, Egypt, Morocco and Tunisia), 1964 to 2009 when financial development is proxy by the banking system, the period 1988–2009 for the second proxy related to the stock market.	FD indicators: Regarding the banking system: 1- the ratio of the bank deposit to nominal GDP 2- private sector credit to nominal GDP Regarding the stock market: 1- Market capitalisation to GDP 2- The ratio of value shares traded to GDP turnover value EG Indicator: real GDP per capita	Cointegration analysis: 1- panel unit root tests 2- Pedroni panel cointegration test 3- panel fully modified ordinary least squares (FMOLS) method.

(Valickova, Havranek, and Horvath 2015) 1334 estimates from 67 studies	<u>FD Indicators:</u> 1- Financial Depth: * the ratio of liquid liabilities of the financial system to GDP * the ratio of M3 to GDP 2- Bank Ratio: * the ratio of bank credit to the sum of bank credit and domestic assets of the central bank 3- Financial Activity * the ratio of private domestic credit provided by deposit money banks to GDP * the ratio of private domestic credit provided by deposit money banks and other financial institutions to GDP * the ratio of credit allocated to private enterprises to total domestic credit 4- Stock market development: * the market capitalisation ratio (the total value of listed shares relative to GDP) * stock market activity (he total value of traded shares relative to GDP) * the turnover ratio (the total value of traded shares relative to the total value of listed shares) <u>FD Indicators (alternative measures):</u> * the aggregate measure of overall stock market development * the share of resources that the society devotes to its financial system * the ratio of deposit money bank assets to GDP	multivariate meta-regression analyses

	* the ratio of bank credit to bank deposits	
(Akinci, Akinci, and Yilmaz 2014) Panel data of OECD member countries for the period 1980-2011	<u>FD Indicators:</u> 1- domestic credits (DC) by the banking sector as a percentage of GDP 2- the ratio of broad measure of money, namely M2, to GDP 3- the ratio of total bank deposits to GDP 4- the ratio of financial system deposits to the GDP <u>EG Indicator:</u> The percentage change of GDP in constant prices	unbalanced panel cointegration and causality analysis the Pedroni and Kao Cointegration Analysis Vector Error Correction Model (VECM)
(Grassa and Gazdar 2014) five GCC countries (Bahrain, Kuwait, Qatar Saudi Arabia and UAE) over the period of 1996-2011	<u>EG Indicator:</u> real per capita GDP growth <u>FD Indicators:</u> 1- private credit (CRE); equals banking institution credit to private sector as a percentage of GDP 2- Deposit money banks (DEPO); equals the ratio of the total assets of deposit money banks divided by GDP 3- Sukuk to GDP ratio; equals total Sukuk issued as a percentage of GDP <u>Control variables:</u>	generalised least squares, OLS and panel data frameworks

	1- Initial level of development (IIC): equals the logarithm of initial income per capita, 2- Trade openness (TO): the ratio of the sum of exports and imports over GDP 3- Secondary school enrollments (SSCE) 4- Government consumption (GC): the ratio of GC to GDP.	
(Tabash and Dhankar 2014) Time series data from 1990 to 2008 of Qatar, Bahrain, and United Arab Emirates (UAE), are selected for the study.	FD Indicators: 1- Islamic banks' financing credited to private sector through modes of financing EG Indicator: Gross Domestic Product (GDP)	the unit root test, co-integration test and Granger causality tests
(Hachicha and Ben Amar 2015) Malaysia from 2000Q1 to 2011Q4.	Control Variables: 1- Capital and labour FD indicators: 1- the ratio of the outstanding loans granted by the Islamic banks to the total outstanding bank loans (Islamic and non-Islamic) granted to the private sector 2- the ratio of the bank loans granted to the private sector by the Islamic banks to the GDP	Error-Correction Model

	3- the ratio of the loans granted by the Islamic Financial Intermediaries to private investments EG Indicators: the real GDP (on Purchasing Power Parity (PPP))	
(Samargandi *et al.* 2015) a panel of 52 middle-income countries over the 1980–2008 period	Control variables: 1- initial real GDP, 2- gross fixed capital formation 3- population growth, 4- openness to trade 5- government expenditure as a share of GDP, 6- life expectancy 7- inflation FD indicators: 1- the ratio of liquid liabilities (or M3) to nominal GDP; 2- the ratio of commercial bank assets to the sum of commercial bank assets and central bank assets, 3- the ratio of bank credit to the private sector to GDP. EG Indicator: growth rate of real GDP	The error-correction model using the autoregressive distributed lag ARDL(p,q) technique Principal components analysis (PCA) The use of a panel ARDL model based on the use of three alternative estimators: 1- mean group estimator (MG) of Pesaran and Smith (1995), 2- pooled mean group estimator (PMG), 3- dynamic fixed effects (DFE) estimator developed by Pesaran *et al.* (1999).

Table A.2.10 Report for Hausman Test Results

--- Coefficients ----

	(b) fixed	(B) Random	(b-B) difference	sqrt(diag(V_b-V_B)) S.E.
gdppcg	-.0004048	-.0004589	.0000541	.
trade	-.0000248	.0000256	-.0000504	.
oilrent	-.0009648	-.0007754	-.0001894	.
indusgdp	.2919914	.2500222	.0419692	.0348617
rol	.0001775	.0004375	-.0002601	.0000436
polsta	-.0003972	-.0002596	-.0001376	.
cbankcrdt	.0003506	.0004516	-.000101	.
istfin	.0568732	.0566393	.0002339	.

b = consistent under Ho and Ha; obtained from xtreg

B = inconsistent under Ha, efficient under Ho; obtained from xtreg

Test: Ho: difference in coefficients not systematic

chi2(**8**) = (b-B)'[(V_b-V_B)^(-1)](b-B)

= **198.93**

Prob>chi2 = **0.0000** (V_b-V_B is not positive definite)